Telstra

# innovation – making thinking work

Annual Report 2005

We are providing our report to shareholders in two parts:

- Annual Review 2005; and
- Annual Report 2005

Both parts will be lodged with the Australian Stock Exchange (ASX) and the Australian Securities and Investments Commission (ASIC) and are available on the Internet:

**http://www.telstra.com.au/abouttelstra/investor/annual_reports.cfm**

This Annual Report is a detailed report that has been prepared by Telstra Corporation Limited as part of its statutory annual reporting obligations under section 314 of the Australian Corporations Act 2001 (Cwth). The Annual Report does not represent or summarise all publicly available information in relation to Telstra. There is other publicly available information in relation to Telstra that has been notified to the ASX and ASIC. Some of this information has also been lodged with the United States Securities and Exchange Commission (SEC). Copies of documents lodged with the ASX and ASIC may be obtained from ASIC and copies of documents lodged with the SEC may be obtained from the SEC.

Nothing in this Annual Report is or shall be taken to be an invitation or an application or an offer to subscribe for, or buy shares in, Telstra.

Terms used in this report:

- **We, Telstra, Telstra Group and the Company** – all mean Telstra Corporation Limited, an Australian corporation, and its controlled entities as a whole; and
- **Telstra entity** is the legal entity, Telstra Corporation Limited.

Our fiscal year ends on 30 June. Unless we state differently, the following apply:

- **Year** or a **fiscal year** means the year ended 30 June; and
- **2005** means **fiscal 2005** and similarly for other fiscal years.

All amounts are expressed in Australian dollars (A$) unless otherwise stated.

A glossary of other terms used is provided to assist with the general understanding of the report.

**Telstra Corporation Limited**
Australian Business Number: 33 051 775 556
Registered Office: 41/242 Exhibition Street
Melbourne Vic 3000
Australia

# Contents

# Contents

# Summary Overview

## General

We are Australia's leading telecommunications and information services company, with one of the best known brands in the country. We offer a full range of services and compete in all telecommunications markets throughout Australia and certain overseas countries.

Our main activities include the provision of:

- basic access services to most homes and businesses in Australia;
- local and long distance telephone calls in Australia and international calls to and from Australia;
- mobile telecommunications services;
- broadband access;
- a comprehensive range of data and Internet services (including through Telstra BigPond®, Australia's leading Internet service provider (ISP));
- management of business customers' IT and/or telecommunications services;
- wholesale services to other carriers, carriage service providers (CSPs) and ISPs;
- advertising, search and information services; and
- cable distribution services for FOXTEL's cable subscription television services.

Our international business includes Hong Kong CSL Limited (CSL), one of Hong Kong's leading mobile operators, TelstraClear Limited (TelstraClear), the second largest full service carrier in New Zealand and Reach Ltd (REACH), a provider of international voice and satellite services in Asia.

One of our major strengths in providing integrated telecommunications services is our extensive geographical coverage through both our fixed and mobile network infrastructure. This network and systems infrastructure underpins the carriage and termination of the majority of Australia's domestic and international voice and data telephony traffic.

Our vision is to be Australia's connection to the future. Our mission is to develop, design and deliver great communications solutions to all our customers. Our goal is to grow the Company profitably and provide attractive returns to our shareholders. We will achieve this by employing terrific people who work together in an operationally excellent way to deliver innovative products and outstanding service to our customers.

# Key Information

## Selected financial data

We recommend that the following information be read in conjunction with our financial statements, the accompanying notes to our financial statements and other information included in this annual report.

Our selected financial data is derived from our audited consolidated financial statements and accompanying notes to our financial statements, which were prepared in accordance with Australian GAAP. Where this differs in material respects from USGAAP, these differences are shown in note 30 to the financial statements.

### Financial data

| | Year ended 30 June | | | | | |
|---|---|---|---|---|---|---|
| | **2005** | **2005** (1) | **2004** | **2003** | **2002** | **2001** |
| | (in millions, except per share amounts) | | | | | |
| | **A$** | **US$** | **A$** | **A$** | **A$** | **A$** |
| **Statement of Financial Performance Data** | | | | | | |
| ***Amounts in accordance with Australian GAAP*:** | | | | | | |
| Revenue from ordinary activities (2) | **22,760** | **17,338** | 21,335 | 21,700 | 20,928 | 23,086 |
| Expenses from ordinary activities (excluding depreciation, amortisation and borrowing costs) (2) (3) | **11,886** | **9,054** | 11,105 | 12,446 | 11,319 | 13,149 |
| Depreciation and amortisation | **3,766** | **2,869** | 3,615 | 3,447 | 3,267 | 2,871 |
| Borrowing costs | **839** | **639** | 767 | 879 | 896 | 769 |
| Profit before income tax expense | **6,269** | **4,776** | 5,848 | 4,928 | 5,446 | 6,297 |
| Net profit | **4,447** | **3,388** | 4,117 | 3,394 | 3,650 | 4,061 |
| Net profit available to Telstra Entity shareholders | **4,447** | **3,388** | 4,118 | 3,429 | 3,661 | 4,058 |
| Earnings per share (4) | **0.36** | **0.27** | 0.32 | 0.27 | 0.29 | 0.32 |
| Earnings per American depositary share (ADS) (4) | **1.80** | **1.35** | 1.60 | 1.35 | 1.45 | 1.60 |
| Dividends paid (5) | **4,131** | **3,147** | 3,186 | 3,345 | 2,831 | 2,316 |
| Dividends declared for the fiscal year | **4,978** | **3,792** | 3,284 | 3,474 | 2,830 | 2,445 |
| Dividends declared per share | **0.40** | **0.30** | 0.26 | 0.27 | 0.22 | 0.19 |
| Dividends per ADS (6) | **2.00** | **1.50** | 1.30 | 1.35 | 1.10 | 0.95 |
| ***Amounts in accordance with USGAAP:*** | | | | | | |
| Operating revenue | **22,167** | **16,887** | 20,737 | 20,495 | 20,196 | 19,456 |
| Net income | **4,172** | **3,179** | 1,381 | 3,450 | 3,898 | 3,576 |
| Basic earnings per share (4) | **0.34** | **0.26** | 0.11 | 0.27 | 0.31 | 0.28 |
| Basic earnings per ADS (4) | **1.70** | **1.30** | 0.55 | 1.35 | 1.55 | 1.40 |
| Dividends per ADS (6) | **US$1.27** | | US$0.90 | US$0.77 | US$0.58 | US$0.46 |
| **Statement of Financial Position Data (at year end)** | | | | | | |
| ***Amounts in accordance with Australian GAAP:*** | | | | | | |
| Total assets | **36,310** | **27,660** | 34,993 | 35,599 | 38,219 | 38,003 |
| Current interest-bearing liabilities | **1,518** | **1,156** | 3,246 | 1,323 | 1,896 | 2,604 |
| Non current interest-bearing liabilities | **11,816** | **9,001** | 9,014 | 11,232 | 12,481 | 11,915 |
| Contributed equity | **5,793** | **4,413** | 6,073 | 6,433 | 6,433 | 6,433 |
| Shareholders' equity/net assets | **14,881** | **11,336** | 15,361 | 15,422 | 14,106 | 13,722 |

# Key Information

| | Year ended 30 June | | | | | |
|---|---|---|---|---|---|---|
| | 2005 | 2005 [1] | 2004 | 2003 | 2002 | 2001 |
| | (in millions, except per share amounts) | | | | | |
| | A$ | US$ | A$ | A$ | A$ | A$ |
| ***Amounts in accordance with USGAAP:*** | | | | | | |
| Total assets | **36,966** | **28,160** | 35,580 | 40,422 | 42,719 | 42,561 |
| Current borrowings | **1,524** | **1,161** | 3,246 | 1,323 | 1,866 | 2,604 |
| Non current borrowings | **11,641** | **8,868** | 9,095 | 11,580 | 12,372 | 11,943 |
| Share captial | **5,921** | **4,511** | 6,164 | 6,568 | 6,536 | 6,455 |
| Shareholders equity/net assets | **14,367** | **10,945** | 15,291 | 18,025 | 18,402 | 17,795 |
| **Revenue from ordinary activities comprises:** | | | | | | |
| Sales revenue | **22,161** | **16,882** | 20,737 | 20,495 | 20,196 | 18,679 |
| Interest revenue | **103** | **78** | 55 | 84 | 126 | 103 |
| Revenue from sale of assets and investments | **226** | **172** | 330 | 859 | 302 | 3,303 |
| Dividend revenue | **-** | **-** | 1 | 1 | 1 | 16 |
| Miscellaneous revenue | **270** | **206** | 212 | 261 | 303 | 985 |
| | **22,760** | **17,338** | 21,335 | 21,700 | 20,928 | 23,086 |

(1) *Unless otherwise noted, all amounts have been translated at the noon buying rate on 30 June 2005 of A$1.00 = US$0.7618.*

(2) *For a breakdown of operating revenue by product group and a breakdown of operating expenses by expense category, see 'Operating and Financial Review and Prospects'.*

(3) *Includes our share of net (profit)/loss from joint venture entities and associated entities.*

(4) *Calculated based on the weighted average number of issued ordinary shares that were outstanding during the fiscal year and, in the case of ADS calculations, based on a ratio of five shares per ADS. As at 30 June 2005, we had issued ordinary shares of 12,443,074,357 after completing a share buy-back during fiscal 2005 of 185,284,669 ordinary shares. As at 30 June 2004, we had issued ordinary shares of 12,628,359,026 after completing a share buy-back during fiscal 2004 of 238,241,174 ordinary shares. During fiscal 2001 to fiscal 2003, we had 12,866,600,200 issued ordinary shares at the end of each year. Basic earnings per share for each year were the same as diluted earnings per share.*

(5) *During fiscal 2005, we paid dividends of A$4,131 million, being the previous year's final dividend of A$1,642 million, the fiscal 2005 interim dividend of A$1,742 million and a special dividend of A$747 million paid with the interim.*

(6) *Calculated based on dividends paid during the year on a ratio of five shares per ADS.*

## Exchange rate information

Our consolidated financial statements are shown in Australian dollars (A$) except where another currency is specified. For convenience, this report has translations of certain A$ into US dollars (US$) at an exchange rate as at 30 June 2005 of A$1.00 = US$0.7618. These translations are indicative only and do not mean that the A$ amounts could be converted to US$ at the rate indicated.

The tables below show the rates of exchange at the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York:

- at the latest practicable date before the publication of this annual report, being 18 August 2005: A$1.00 = US$0.7537;
- the high and low exchange rates for six months preceding the date of this annual report:

| | High | Low |
|---|---|---|
| February 2005 | 0.7940 | 0.7669 |
| March 2005 | 0.7974 | 0.7685 |
| April 2005 | 0.7834 | 0.7658 |
| May 2005 | 0.7810 | 0.7550 |
| June 2005 | 0.7792 | 0.7498 |
| July 2005 | 0.7661 | 0.7403 |

# Key Information

- for the five most recent fiscal years:

| Year ended 30 June | At period end | Average rate(1) | High | Low |
|---|---|---|---|---|
| 2001 | 0.5100 | 0.5372 | 0.5996 | 0.4828 |
| 2002 | 0.5628 | 0.5240 | 0.5748 | 0.4841 |
| 2003 | 0.6713 | 0.5884 | 0.6729 | 0.5280 |
| 2004 | 0.6952 | 0.7155 | 0.7979 | 0.6930 |
| 2005 | 0.7618 | 0.7568 | 0.7974 | 0.6880 |

(1) *The average of the noon buying rates on the last day of each month during the year.*

Fluctuations in the A$ to US$ exchange rate will affect:

- the US$ equivalent of the A$ price of our shares on the Australian Stock Exchange (ASX). Consequently, this is likely to affect the market price of our American depositary shares (ADS) in the US; and
- the US$ amounts received by holders of ADS on conversion by the Depositary of cash dividends paid in A$ on the shares underlying the ADS.

## Risk factors

The following describes some of the significant risks that could affect us. Additionally, some risks may be unknown to us and other risks, currently believed to be immaterial, could turn out to be material. All of these could materially adversely affect our business, profits, assets, liquidity and capital resources. They should be considered in connection with any forward-looking statements in this annual report and the warning regarding forward-looking statements in this section of this annual report.

***Strategic review requested by the Board***

Telstra is a fully integrated telecommunications company with complex business processes and systems, which have been developed on the premise of certain strategic objectives and agendas.

On 1 July 2005 Solomon Trujillo commenced as our new CEO, replacing Ziggy Switkowski who had been CEO for six years. Our new CEO is currently conducting a strategic review of our operations and strategies under the Board's instructions. There is a risk that as a result of this strategic review we may implement changes to our previous strategies requiring significant investment in new technology and systems and the development of new products and services, which may affect our financial position. For a fuller discussion see 'Operating and Financial Review and Prospects – Overview of key factors affecting our business and financial performance'.

***The further privatisation of Telstra may impact our operations***

The Government has recently stated that it will introduce legislation to enable the further sale of its remaining interest in us. In March 2005, the Government appointed external business advisers to undertake a scoping study to assess the possibility of a sale and to make recommendations to the Government.
The objective of the scoping study was to produce a comprehensive report addressing commercial, policy, regulatory, financial, industry, project management and other issues relevant to divesting the Commonwealth's remaining interest in us. The scoping study was completed in June 2005 and advised that the preferred timing for any sale of the Commonwealth's remaining interest in us is late 2006.
The Government has stated that it will make a further decision in early 2006 about proceeding with a sale. This decision will include an assessment of whether the level of demand for the shares would allow a partial or full sale of the Commonwealth's remaining interest in us. Until this decision is made by the Government and announced, it is unclear how this may affect our capital structure, operations, organisational structure

## Key Information

and corporate compliance obligations. Any sale by the Commonwealth of its remaining interest in us may involve substantial use of management time and resources, as well as expenditure on external advisers. For further information regarding our shareholders, see ‘Major Shareholders and Related Parties’.

***We are subject to extensive regulation that may negatively affect our business and profitability by constraining our ability to pursue certain business opportunities and activities affecting the returns we can generate on our assets.***

We operate in a heavily regulated environment. Australia has generally applicable and established competition law. There is further telecommunications-specific legislation that regulates matters such as carrier and CSP obligations, industry specific competition regulation and those of our services to which competitors can have access (and the terms and conditions under which we provide this access). We are also subject to regulations that are specific to us and not applicable to our competitors. For example, under the Telstra Corporation Act 1991 (Cwth) (Telstra Act), the Communications Minister may direct us to act in particular ways that benefit the public interest even though those actions may not be in our best commercial interests.

The current Commonwealth Government has stated that it is considering selling its remaining interest in us. The Government has indicated that any sale legislation will form part of a package of legislation which will give effect to a number of regulatory reforms including the introduction of an Australian model of operational separation that will apply to our internal structure. See risk factor regarding further privatisation of Telstra.

Because of these numerous factors, there is a risk that we could be exposed to significant limitations, uncommercial imposts, penalties and compensation payments in relation to our current and future activities and assets. This may make it prudent on some occasions for us to cease or choose not to engage in business activities in which we might otherwise engage or avoid, or defer or abandon certain capital projects. These regulatory risks could therefore have an adverse effect on our ability to pursue certain business opportunities and activities and the returns we can generate on our assets. This may in turn adversely affect our financial performance.

For more information regarding our regulatory environment and our obligations and potential liabilities under Australian and overseas regulations, see ‘Competition and Regulation - Regulation’.

***We are subject to new financial reporting obligations***

The Australian Accounting Standards Board (AASB) has adopted International Financial Reporting Standards (IFRS) for application to reporting periods beginning on or after 1 January 2005. The AASB has issued Australian equivalents to IFRS (A-IFRS), which will be reflected in the financial statements for the first time for the half-year ending 31 December 2005 and the year ending 30 June 2006.

Under A-IFRS, we expect our net profit after tax to be more volatile compared with our existing Australian reporting requirements. However, we expect that the adoption of A-IFRS will not affect our net cash flow, our ability to borrow funds or our capacity to pay dividends to our shareholders.

Refer to note 1.4 to our financial statements for further details regarding our adoption of A-IFRS.

***Competition in the Australian telecommunications market could cause us to continue to lose market share and reduce our prices and profits from current products and services***

The Australian telecommunications market has become increasingly competitive since the Commonwealth Government introduced open competition on 1 July 1997. Although the overall market has experienced growth to date, we have lost substantial market share in some key markets. In response to increased

# Key Information

competition, we have lowered the prices of our products and services, particularly the prices for our local calls, national long distance calls and international telephone services and calls to and from mobile services. We expect that these trends will continue due to competitive activity, regulation requiring reductions in call prices and regulatory facilitation of access to our networks, products and services.

We expect competitors to continue to engage in vigorous price competition. We also expect that our competitors will continue to market aggressively to those of our customers who purchase large volumes of telecommunications services from us. The continued loss of market share could have an adverse effect on our financial results in the market or markets in which this type of competition occurs.

For more information on our competitive environment, see ‘Competition and Regulation - Competition’.

***If growth in mobiles and some of our other products continues to slow, our revenues may not increase as rapidly as in the past and may even decrease, which in turn could adversely affect our profitability***

In recent years, our revenues have increased in a large part because of rapid usage growth in new services such as mobile communications, data, Internet products as well as advertising and directories services, whilst revenue for PSTN services declined. Indications are that some of these product markets are not likely to continue expanding at the same rates, as in recent years, and may decline. If these markets do not continue to expand, then in the absence of new products and services our revenue growth may continue to slow just as some revenue growth declined in the second half of fiscal 2005, which in turn could affect our consolidated financial position and results of operations.

***Rapid technological changes and the convergence of traditional telecommunications markets with data, Internet and media markets expose us to significant operational, competitive and technological risks***

Rapid changes in telecommunications and IT are continuing to redefine the markets in which we operate, the products and services required by our customers and the ability of companies to compete in the telecommunications industry in Australia and elsewhere in the world. These changes are likely to broaden the range, reduce the costs and expand the capacities and functions of infrastructure capable of delivering these products and services.

As traditional telecommunications, data, Internet and media markets converge, it is possible that further new competitors may enter the markets in which we have traditionally competed and we may confront established competitors in new markets we seek to enter. This could result in reduced market share, revenue and profitability in our traditional markets and could adversely affect our ability to win market share and operate profitably in these new markets.

To address the converging telecommunications, data, Internet and media markets, we may be required to devote considerable resources to enhancing our ability to deliver services required by these markets. There is a risk that competitors may leverage both their own and our infrastructure or deploy or develop technologies or infrastructure that provides them with a lower cost base or other operating advantages that may drive down market prices. This could give these competitors an advantage if we are unable to promptly and efficiently provide equivalent services. We have invested substantial capital and other resources in the development and modernisation of our networks and systems. However, we may be required to incur significant capital expenditures in addition to those already planned in order to remain competitive. This will also require careful management of the existing asset base, as well as careful consideration of the appropriate decisions on technology investment. There is a risk that our ability to respond quickly to technological change may be hampered by the complexity of integrating our existing systems with new technologies.

# Key Information

Rapid changes in telecommunications and IT could also have an impact on the useful lives of our communications assets. We assess the appropriateness of the service lives of our communications assets on an annual basis. This assessment includes a determination of when the assets may be superseded technologically. We use an "end date lifing" methodology where we believe that technologies will be replaced by a certain date. If our assessments of useful lives prove to be incorrect, we may incur either higher or lower depreciation charges in the future or, in certain circumstances, be required to write down these assets.

***Our ability to develop, build and maintain products to satisfy market demand may not be realised***

In order to meet market demand, we constantly develop, build and maintain our products to satisfy our customers' needs. Due to the multiplicity of products in the market, there is a risk that we may incorrectly predict future market demand for certain products which we develop and maintain. There is a risk that the profitability of certain products may decline if customers choose alternative products. For a detailed description of our products and services see 'Information on the Company – Products and services'.

***Innovations in technology may require us to transform our existing organisational structure, cost structure, people skills, and infrastructure asset values***

Our revenues, products and costs are changing as a result of lower technological barriers to entry, margin pressures and increased regulatory scrutiny. The need to transform the company to new operational models will become important for profitable growth. The company faces challenges in transforming into an IP enabled environment and generating efficiencies and profitable growth. There is a risk that this challenge may require the transformation of our organisational structure, cost structure, people skills and ongoing asset values for existing infrastructure which could negatively affect our operating cost structures.

***Network and system failures and planning inaccuracies could result in reduced user traffic, reduced revenue and harm to our reputation***

Our technical infrastructure is vulnerable to damage or interruption from floods, wind storms, fires, power loss, telecommunication failures, cable cuts, intentional wrongdoing and similar events. The networks and systems that make up our infrastructure require regular maintenance and upgrade that may cause disruption. The occurrence of a natural disaster or other unanticipated problems at our facilities or any other damage to or failure of our networks and/or systems could result in consequential interruptions in service across our integrated infrastructure. Network and/or system failures, hardware or software failures or computer viruses could also affect the quality of our services and cause temporary service interruptions.

Periodically we also make assessments of our major customers' capacity requirements especially when we move them to new platforms to ensure that their capacity requirements will be satisfied. There is a risk that our capacity planning may not accurately predict their actual requirements

Our IT systems are complex and there is a risk that our ability to support strategic priorities in customer service and growth products may be delayed by the complexity of changing our systems. Our IT systems are also vulnerable to viruses, denial of service and other similar attacks which may damage our systems and data and that of our customers. Any of these occurrences could result in customer dissatisfaction and damages or compensation claims as well as reduced revenue.

***Further technological innovations and cost pressures may cause us difficulty in retaining and attracting skilled and experienced people***

As technology evolves further we will need to attract, retain and up-skill our workforce to keep abreast of technological innovations. The relevant skills may be in short supply worldwide until the leading edge technology is fully established. There is a risk that an inability to compete in the global labour market

## Key Information

may hinder our ability to retain and attract skilled and experienced people and hence to embrace new technology and retain our corporate knowledge. For more information on our workforce, see 'Directors, Management and Employees'.

***Our ability to pursue our strategy with respect to some investments in which we share control or do not own a controlling interest may be limited***

Some of our domestic Australian and international activities are conducted through subsidiaries, joint venture entities and other equity investments. Under the governing documents for some of these entities, certain key matters such as the approval of business plans and decisions as to the timing and amount of cash distributions require the agreement of our co-participants. Our co-participants may have different approaches with respect to the investment and the markets in which they operate and on occasions we may be unable to reach agreement with them.

In some cases, strategic or venture participants may choose not to continue their participation. In addition, our arrangements with our co-participants may expose us to additional investment, capital expenditure or financing requirements. There are also circumstances where we do not participate in the control of, or do not own a controlling interest in, an investment and our co-participants may have the right to make decisions on certain key business matters with which we do not agree.

All of these factors could negatively affect our ability to pursue our business strategies with respect to the concerned entities and the markets in which they operate. For more information on some of our investments, see 'Information on the Company - International investments' and 'Information on the Company - Products and services - Mobiles - 3G wireless service' and 'Information on the Company – Products and services – Subscription television'.

***The value of our operations and investments may be adversely affected by political and economic developments in Australia or other countries***

Our business is dependent on general economic conditions in Australia, including levels of GDP, interest rates and inflation. A significant deterioration in these conditions could adversely affect our business and results of operations. We may also be adversely affected by developments in other countries where we have made equity investments or entered into ventures such as Asia, including Hong Kong, and New Zealand. Important features of the political, economic, regulatory and legal systems in these countries are different from those in Australia. Other countries in which we have interests may additionally have less predictable political, economic, regulatory and legal environments. As a result, our international operations may be subject to numerous unique risks, including:

- multiple and conflicting regulations regarding communications, use of data and control of Internet access;
- changes in regulatory requirements, import and export restrictions and tariffs;
- changes in the relevant authorities' interpretation of what conduct constitutes appropriate compliance with regulatory requirements, and consequent changes in regulatory enforcement;
- market changes and competitors' initiatives such as bundling of services and deep discounting;
- the burden of complying with the laws of a variety of jurisdictions;
- access to additional capital;
- fluctuations in currency exchange rates and interest rates;

# Key Information

- the introduction of new restrictions on repatriation of profits and permitted foreign ownership, or changes to existing restrictions;
- changes in political and economic stability;
- potentially adverse tax consequences; and
- inadequate protection for intellectual property rights and enforcement of those rights in certain countries.

These factors could materially and adversely affect our future revenues, operating results and financial condition.

***Fluctuations in currency exchange rates may adversely affect our revenues, operating results and the translation value of our overseas investments***

Because we purchase some materials and supplies with prices dependent on foreign currencies and have substantial international investments denominated in foreign currencies, movements in the value of the A$ against other currencies can adversely affect our performance including revenues, operating results and balance sheet amounts. For the fiscal year ended 30 June 2005, approximately 7% of our revenues, 73% of our underlying borrowings and 8% of our total assets were denominated in or dependant on currencies other than the A$ prior to hedging.

While the majority of our foreign currency exposures associated with our borrowings is fully hedged to A$, we partially hedge exposures to purchases and translation risk associated with our core business activities including investments, generally to around fifty percent of the value. We enter into hedge transactions of these exposures principally to reduce the volatility of exchange rate movements on our financial performance and results. Foreign currency exposure associated with the purchase of materials and the supply of goods and services is also generally hedged to around fifty per cent of the value, although in certain circumstances, depending on the size and nature of the exposure, the level of hedging may vary.

Whilst we undertake risk management strategies to mitigate the adverse impact of foreign currency exposures, there is a risk that currency movements could still negatively affect our operating results or financial position.

More information on our exposure to risk from foreign currency exchange rate fluctuations is provided in ‘Quantitative and Qualitative Disclosures about Market Risk’.

## Cautionary statement regarding “forward-looking statements”

Some of the information contained in this annual report may constitute forward-looking statements that are subject to various risks and uncertainties. These statements can be identified by the use of forward-looking terminology such as ‘may’, ‘will’, ‘expect’, ‘anticipate’, ‘estimate’, ‘continue’, ‘plan’, ‘intend’, ‘believe’ or other similar words. These statements discuss future expectations concerning results of operations or of financial condition or provide other forward-looking information. Our actual results, performance or achievements could be significantly different from the results expressed in, or implied by, those forward-looking statements. Important factors that could cause our actual results to differ materially from the forward-looking statements we make in this annual report are set forth above under the caption ‘Risk factors’ and elsewhere in this annual report. Given these risks, uncertainties and other factors, you should not place an undue reliance on any forward-looking statement, which speaks only as of the date made.

# Information on the Company

## History and development of the Company

Our origins date back to 1901, when the Postmaster-General's Department was established by the Commonwealth Government to manage all domestic telephone, telegraph and postal services, and to 1946, when the Overseas Telecommunications Commission was established by the Commonwealth Government to manage international telecommunications services. Since then, we have been transformed and renamed several times as follows:

- the Australian Telecommunications Commission, trading as Telecom Australia, in July 1975;
- the Australian Telecommunications Corporation, trading as Telecom Australia, in January 1989;
- the Australian and Overseas Telecommunications Corporation Limited in February 1992;
- Telstra Corporation Limited in April 1993, trading internationally as Telstra; and
- trading domestically as Telstra in 1995.

We were incorporated as an Australian public limited liability company in November 1991. Following the opening of Australia's telecommunications markets to full competition in July 1997, we underwent a partial privatisation in November 1997 under which the Commonwealth sold approximately 33.3% of our issued shares to the public. Following the initial privatisation, those of our shares that are not held by the Commonwealth are quoted on the Australian Stock Exchange (ASX) and on the New Zealand Stock Exchange. ADSs, each representing five shares evidenced by American depositary receipts (ADRs), have been issued by the Bank of New York as depositary (Depositary) and are listed on the New York Stock Exchange (NYSE).

A further global offering by the Commonwealth of up to 16.6% of our issued shares was launched in September 1999. The shares sold by the Commonwealth were also listed on the ASX, the New Zealand Stock Exchange and the NYSE on 18 October 1999. As at 30 June 2005, the Commonwealth owned approximately 51.8% of our issued shares and it is required by legislation to own at least 50.1% of our issued shares.

However, the Government has recently stated that it will introduce legislation to enable the further sale of its remaining interest in us. In March 2005, the Government appointed external business advisers to undertake a scoping study to assess the possibility of a sale and to make recommendations to the Government. The scoping study was completed in June 2005 and advised that the preferred timing for any sale of the Commonwealth's remaining interest in us is late 2006. The Government has stated that it will make a further decision in early 2006 about proceeding with a sale. This decision will include an assessment of whether the level of demand for the shares would allow a partial or full sale of the Commonwealth's remaining interest in us.

## Organisational structure

Our organisational structure consists of strategic business units and corporate centre business units as outlined below.

### Strategic business units

- **Telstra Consumer and Marketing** is responsible for serving metropolitan consumer and small business customers with our full range of products and services including fixed, wireless and data, the overall management of our brands, advertising and sponsorships, consumer marketing and implementing our product bundling initiatives. It also has responsibility for Telstra's Consumer Call Centres, licensed shops and dealer network.

- **Telstra Business and Government** is responsible for providing innovative and leading edge communications and ICT solutions to business and Government enterprises in Australia and New Zealand. It also oversees our investment in TelstraClear. **TelstraClear** is New Zealand's second largest

## Information on the Company

full service telecommunications company, providing innovative market leading products, services and customer focus to the business, government, wholesale and residential sectors.

- **Telstra Country Wide®** is responsible for sales, service and the management of customer relationships in outer metropolitan, regional, rural and remote parts of Australia and the development and delivery of innovative communications solutions to meet the needs of customers living in these areas.
- **Telstra BigPond®** is our retail Internet business and is responsible for providing broadband and narrowband Internet services for consumer and small and medium business customers, as well as value added services and content services (including BigPond® Movies, BigPond® Music, BigPond® Sport, BigPond® Games).
- **Sensis** is a wholly owned subsidiary which is responsible for our advertising, directories and information services.
- **Telstra Media** is responsible for our FOXTEL investment.
- **Telstra Wholesale** provides a wide range of wholesale products and services to the Australian domestic market including fixed, wireless, data and Internet, transmission and IP, interconnection, access to our network facilities, and retail/rebill products. It also offers network design and construction solutions as well as operations and maintenance services, including management and maintenance of integrated IP networks, mobility solutions, fixed access, wireless access and transmission solutions. Recently, Telstra Wholesale has commenced servicing Global Wholesale markets to satisfy growing Internet and high bandwidth needs.
- **Telstra Asia** manages our international interests in Asia, including CSL and our joint venture REACH in Hong Kong. It also directs our offshore growth strategy, with a current focus on enhancing the value of our existing investments, profitably rationalising non-core assets and positioning us to capture high growth opportunities in the region, particularly China and South East Asia.
- **Infrastructure Services** builds, operates and maintains our telecommunications infrastructure and is our primary service delivery manager. It is responsible for the provisioning, restoration, operation and management of our fixed, mobile, IP and data networks, as well as the design and construction of network infrastructure. This includes voice and data, product and application platforms and the online environment. Over the past year Infrastructure Services' capability has been augmented by the 3GIS joint- venture with Hutchison and the integration of Telstra Business Systems (formerly Damovo (Australia)).
- **Telstra Technology Innovation and Products** is responsible for the management of all technology, platform and product delivery. It develops and supports products and technologies specified by our market facing business units. It also undertakes substantial research and development to ensure that we remain at the forefront of technology in Australia.

## Information on the Company

### Corporate centre business units

- **Finance & Administration** is responsible for corporate policy and support functions including finance, risk management and assurance, credit management, treasury, company secretary, investor relations, mergers and acquisitions and other corporate services. It is also responsible for the financial management of the majority of our fixed assets, including network assets.
- **Legal Services** provides operational and strategic legal support and advice across the Company, with lawyers from Legal Services integrated with the other strategic and corporate centre business units.
- **Public Policy and Communications** is responsible for the management of all our regulatory issues, including liaison with regulatory bodies, the promotion and protection of our reputation by facilitating effective engagement of internal and external stakeholders, including the media, and the management of our interaction with Government at the Commonwealth and State level.
- **Human Relations** is responsible for all our human relations matters including health, safety and the environment, leadership development and training, and all workplace relations matters.

In August 2005, we announced further changes to our organisational structure. We appointed a Chief Operations Officer (COO) to oversee all functions associated with the operational aspects of the Company. The new COO group will comprise the existing Infrastructure Services and Telstra Technology, Innovation and Products business units. It will also include corporate services, credit management, human relations, the productivity and billing directorates, as well as the teams responsible for technology solutions, billing and process improvement elsewhere in the Company. In addition, a new program office will be established and report to the COO. Its mission will be to identify and prioritise opportunities for streamlining, implementing and co-ordinating all aspects of the company's operations in order to deliver the best possible customer service, at the least cost.

Our organisational structure for financial reporting purposes has evolved over recent years to meet our business needs and has included the following:

- in fiscal 2005, we restructured our pre-existing business unit known as Telstra Broadband and Media. This restructure primarily involved the establishment of Telstra Bigpond®, Telstra Media and Sensis as separate business units. These business units are not reportable business segments in their own right and they were included in the "Other" segment for financial reporting purposes; and
- in fiscal 2004, we established Telstra Technology Innovation and Products which brought together product development areas, network technologies, IT systems and Telstra Research Laboratories. Previously, network technologies, IT systems and Telstra Research Laboratories were not managed as a single business segment. The combination of these business areas has created a business unit that is of sufficient size to qualify as a segment in its own right for financial reporting purposes.

Those business units not impacted by the above restructure are substantially consistent to their structure in prior years. See 'Operating and Financial Review and Prospects - Segment information' for a discussion of the financial performance of our reportable segments during the last three fiscal years. Note 5 to our financial statements also provides detailed financial information on our business segments.

A list of our controlled entities is provided in note 23 to our financial statements. Our joint venture entities and associated entities are listed in note 24 to our financial statements.

# Information on the Company

## Marketing and customer service

From supplying Australia's largest public and private sector organisations, to supporting customers using our services at home, we are Australia's leading fully-integrated telecommunications company.

We use sophisticated customer analytics to target services based on customers' needs, giving us a better understanding of their needs and improving relationships to gain a key competitive advantage.

### Residential customers and small businesses

We segment our residential customers based upon their usage and lifestyle patterns. We segment our small business customers according to the type of business they operate and the way they interact with their customers. This information on customers by segment is then used to tailor our marketing campaigns.

We enable customers to interact with us online, through door-to-door sales representatives and telephone sales channels and face to face via our Telstra Shops, Telstra licensed stores, Telstra Business Shops and indirectly through approximately 4,000 retail outlets nationwide in conjunction with our retail partners. This is now managed by our Branded and Indirect Channels Group which was established on 1 July 2005.

### Medium and large businesses and Governments

We segment our customers based on communications spend, 'Telstra Share of Wallet', industry sector and geographic proximity. The three key segments are Government, Industry (our largest corporate customers) and Business (our medium and smaller business customers). We focus on delivering account management and communications solutions to all these customers with the aim of improving our customers' financial performance and business efficiency.

### Regional, rural and remote customers

Telstra Country Wide® was established to improve service levels, business performance and to strengthen relations with customers and communities in regional, rural and remote areas of Australia. In 2003 this area was expanded to include outer metropolitan areas. Area General Managers are located throughout Australia to address the sales, marketing and service needs of our customers.

### Wholesale customers

Our wholesale customers include licensed carriers, CSPs and ISPs. Telstra Wholesale provides products and services to more than 600 customers, including more than 470 ISPs (about 77 of which offer broadband digital subscriber line (DSL) services).

Wholesale customers typically buy products and services from Telstra Wholesale, add their own inputs and then sell to the retail market, under their own brand.

### Advertising customers

Sensis Pty Ltd (Sensis), our wholly owned subsidiary, is a leading Australian advertising, search and information services provider. Sensis provides innovative advertising and local search solutions to more than 420,000 customers nationally, including small and medium enterprises (SMEs), large corporates and Governments through a network of print, online, voice, wireless and in-car services.

Sensis manages three of Australia's leading brands - Yellow Pages®, White Pages® and Trading Post^, along with the CitySearch^ online city guide and the Whereis® mapping and guidance site. Sensis also manages the Sensis® Search portfolio that encompasses the sensis.com.au website and the Sensis® 1234 voice service.

## Information on the Company

### Global business solutions

We have 16 offices around the world including Asia Pacific, Europe and USA supporting the global telecommunications requirements of our multi-national customers and global service providers. Together with our partners and alliances, we can offer our customers access to more than 230 countries and territories across the globe. We have an extensive portfolio of network solutions including dedicated consulting, planning, project management, system integration and customer support seven days a week.

# Information on the Company

## Products and services

We offer a broad range of telecommunications and information products and services to a diverse customer base. The following table shows our operating revenue by major product and service category and as a percentage of total operating revenue for the last three fiscal years. See also 'Operating and Financial Review and Prospects' for a discussion of the revenue performance of our products and services during the last three fiscal years.

***Operating revenue by product and service category, including the percentage of total operating revenue contributed by each product and service category***

| | Year ended 30 June | | | | | |
|---|---|---|---|---|---|---|
| | **2005** | | 2004 | | 2003 | |
| | (in millions, except percentage of revenue) | | | | | |
| | **A$** | % of total | A$ | % of total | A$ | % of total |
| **PSTN products** | | | | | | |
| Basic access | **3,362** | **15** | 3,237 | 15 | 3,083 | 14 |
| Local calls | **1,284** | **6** | 1,504 | 7 | 1,567 | 7 |
| PSTN value added services | **250** | **1** | 259 | 1 | 280 | 1 |
| National long distance calls | **1,013** | **4** | 1,121 | 5 | 1,162 | 6 |
| Fixed to mobile | **1,566** | **7** | 1,597 | 8 | 1,517 | 7 |
| International direct | **234** | **1** | 266 | 1 | 307 | 2 |
| | **7,709** | **34** | 7,984 | 37 | 7,916 | 37 |
| **Mobiles** | | | | | | |
| Mobile services | **3,760** | **17** | 3,470 | 16 | 3,239 | 15 |
| Mobile handsets | **381** | **2** | 352 | 2 | 386 | 2 |
| | **4,141** | **19** | 3,822 | 18 | 3,625 | 17 |
| **Data and Internet services** | | | | | | |
| Internet and IP Solutions | **1,377** | **6** | 1,013 | 5 | 817 | 4 |
| ISDN products | **890** | **4** | 927 | 4 | 942 | 4 |
| Specialised data | **966** | **4** | 1,035 | 5 | 1,059 | 5 |
| | **3,233** | **14** | 2,975 | 14 | 2,818 | 13 |
| **Other products and services** | | | | | | |
| Advertising and directories | **1,585** | **7** | 1,341 | 7 | 1,205 | 6 |
| Intercarrier services | **1,146** | **5** | 1,103 | 5 | 1,136 | 5 |
| Inbound calling products | **449** | **2** | 476 | 2 | 494 | 2 |
| Solutions management | **931** | **4** | 508 | 2 | 501 | 2 |
| Offshore controlled entities | **1,611** | **7** | 1,431 | 7 | 1,544 | 7 |
| Other sales and services | **1,356** | **6** | 1,097 | 5 | 1,256 | 6 |
| | **7,078** | **31** | 5,956 | 28 | 6,136 | 28 |
| Total sales revenue | **22,161** | **98** | 20,737 | 97 | 20,495 | 95 |
| Other revenue [1] (excluding interest revenue) | **496** | **2** | 543 | 3 | 1,121 | 5 |
| Total operating revenue (excluding interest revenue) | **22,657** | **100** | 21,280 | 100 | 21,616 | 100 |

(1) *Other revenue includes miscellaneous revenue and revenue from sale of assets and investments. Interest revenue is included in net borrowing costs.*

## Information on the Company

Sales revenues are derived from domestic and international sales as follows:

| | Year ended 30 June | | |
|---|---|---|---|
| | **2005** | 2004 | 2003 |
| | | (in %) | |
| Australia | 92.3 | 93.1 | 92.5 |
| Hong Kong | 3.5 | 3.5 | 4.4 |
| New Zealand | 3.0 | 2.8 | 2.7 |
| Other International | 1.2 | 0.6 | 0.4 |

No individual country makes a material contribution to sales revenue other than Australia, Hong Kong and New Zealand.

**Basic Access**

We provide Basic Access services to most homes and businesses in Australia and charge our customers fees for new line connections and existing line reconnections. Our Basic Access service includes installing, renting and maintaining connections between customers' premises and our Public Switched Telephone Network (PSTN) and providing basic voice, facsimile (including services marketed under our FaxStream® brand name) and Internet services. Basic Access does not include enhanced products like Integrated Services Digital Network (ISDN) access and Asymmetric Digital Subscriber Line (ADSL) services.

**Local calls (including PSTN value added services)**

We provide local call services to more residential and business customers than any other service provider in Australia, generally charging for calls on an untimed fee basis. In addition, we provide value added services such as voicemail, call waiting, call forwarding, call conferencing and call return.

**National long distance calls**

We are the leading provider of national long distance services for residential and business customers in Australia. This comprises national long distance calls made from our PSTN network to a fixed network. Calls are charged on a timed basis after a call connection fee. Call details such as duration, destination, time of day and day of the week generally determine charges which are also offered on a capped price basis. We also offer options that let customers choose packages to suit individual needs and offer specials to increase use in low demand periods.

**Fixed to mobile**

Fixed to mobile are calls made from our PSTN/ISDN to a mobile network and are charged on a timed basis after a call connection fee. Charges usually depend on the duration of the call and whether the call is to a Telstra mobile service. Calls made within a capped calling option are charged according to duration, time of day, day of week and terminating carrier. Capped calling offers predominantly apply to calls to Telstra mobiles.

**International direct**

We are the leading provider of international telephone services in Australia, offering international telephone services to more than 230 countries and territories. Calls are typically charged on a per second basis after a call connection fee, depending on the duration and destination of the call. REACH provides the connections we use to supply international services to both our retail and wholesale customers. For more information regarding our arrangements with REACH, refer to 'Operating and Financial Review and Prospects - International business ventures'.

# Information on the Company

## Mobiles

We continue to be the leading provider of mobile telecommunications services in Australia in terms of mobile revenue and the number of customers. The geographical coverage area of our network is also very broad. The mobile telecommunications market in Australia is characterised by a significant degree of penetration and we estimate that market penetration as at 30 June 2005 was approximately 90%.

We offer a full range of mobile services to our customers, including voice calling and messaging, text and multimedia messaging and a range of information, entertainment and connectivity services.

During the past year, we have continued to see growth in 'non-voice' services in particular, reflecting a steady change in mobile usage behaviour with new information and entertainment content and connectivity services enjoying significant growth.

We have entered into a strategic partnership with NTT DoCoMo, Inc. under which we have launched i-mode® in Australia. i-mode® is a mobile Internet like service that provides subscribers with access to rich content, email, games and other applications and services through their mobile handsets and has enabled us to take a leading position in the development of a vibrant mobile content industry in Australia.

In addition we are continuing to develop and expand our content services offering for non-i-mode® compatible devices, ensuring that, independent of device choice, customers are still able to access a range of compelling services.

We are also seeing increasing demand for Wireless Connectivity solutions across a range of technologies including WiFi, 1xRTT and recently launched EVDO technologies delivering ever improving price and performance for customers requiring broadband connectivity 'on the move'.

During 2005, we will be offering our first services based on the 3GSM suite of technologies, including WCDMA, delivering both improved performance and new service opportunities such as video communication.

Our wholly-owned subsidiary CSL is also a leading provider of mobile services in Hong Kong. CSL has launched a number of Asian and world first services this year which, together with CSL's history of technical innovation, provides great learning opportunities for us and is anticipated to produce opportunities in the Australian and international markets. For further information on CSL, see 'Information on the Company - International investments'.

### *GSM digital service*

Our digital GSM network covers around 96% of the Australian population and we continue to improve existing areas of coverage and expand this network, where commercially justified. We have also improved depth of coverage in major cities, particularly in-building and underground coverage, as well as offering international roaming in more than 133 countries and 290 networks.

Our 3GSM network, is compatible with our GSM network and will allow additional functionality such as video calling and higher speed data access within its coverage boundary. Our 3GSM network sharing arrangement with Hutchinson covers around 46% of the Australian population in a number of mainland capital cities including Canberra.

### *CDMA digital service*

Our CDMA network provides Australia's largest cellular mobile phone coverage, spanning more than 1.6 million square kilometres and covering more than 98% of the Australian population. CDMA offers advantages over GSM in applications where users require wider service coverage and faster data speed than

## Information on the Company

GSM. Customers are increasingly adopting our CDMA network, which is one of the fastest growing areas of our mobile business.

***Telstra Mobile Satellite***

In 2002, we launched Telstra Mobile Satellite, a hand-held mobile satellite voice and data service for people living, working or travelling in rural and remote Australia. The service operates off the Iridium^ Low Earth Orbit satellite system which provides global mobile satellite phone coverage. We have a service partner agreement to sell the Iridium^ service.

***3G wireless service***

**1XEVDO**

In December 2002, we launched Australia's first commercial mobile network based on CDMA 1X (also known as 1xRTT), on our CDMA network. CDMA 1X is an evolution of CDMA technology supporting high-speed packet-switched data. By the end of 2004 CDMA 1X, also known as Mobile High Speed, was made available across the entire CDMA network footprint of over 1.6 million square km covering over 98% of the population and over 16% of the Australian landmass.

In November 2004 Telstra launched CDMA 1xEVDO within all Australian capital cities and selected regional centres. 1xEVDO offers typical user speeds of 300-600kbps with maximum burst speeds of 2.4Mbps. By the end of August 2005 coverage will have been significantly expanded in Newcastle, Wollongong and the greater Sydney Metropolitan area providing EVDO coverage to over 6 million Australians. Further expansion is also underway for completion in late 2005 within Melbourne and the towns of Bendigo and Seymour.

**3GSM**

We entered into a network sharing agreement with Hutchison 3G Australia (H3GA), a subsidiary of Hutchison Telecommunications (Australia) Ltd, in August 2004 to establish a 50/50 enterprise to jointly own and operate H3GA's existing 3G radio access network and fund future network development. Under the agreement, the H3GA radio access network will become the core asset of the joint enterprise. In return for the 50 per cent ownership of the asset, we will pay Hutchison A$450 million under a fixed payment schedule in four instalments. The first instalment was paid in 2005 and the balance is due to be paid by 1 July 2006.

We will launch our 3G (GSM/WCDMA) services to customers in 2005, utilising the entire H3GA network footprint of more than 2,100 base stations covering Sydney, Melbourne, Brisbane, Adelaide, Canberra and Perth. Telstra and Hutchison expect to significantly increase the size of the network over the next three years, expanding into regional centres. The joint enterprise will open opportunities for new revenues for us and H3GA, stimulate growth in 3G service uptake and provide significant savings in 3G network construction capital expenditure and operating expenses such as site rental and maintenance. Decisions on network development will be made and funded jointly. The joint enterprise will utilise the existing spectrum holdings of both partners and will operate until the expiry of those spectrum licences in 2017 or later.

Telstra and Hutchison will each continue to own separate core networks, application and service platforms, and will conduct their retail 3G businesses independently and in competition with each other.

***Blackberry***

The Blackberry is a wireless service that automatically delivers email to a handheld device via our GSM network. This integrated device is capable of delivering telephony, email, company data, Internet browsing, SMS, calendar and personal organiser features. In March 2005 we launched our Blackberry on CDMA service.

# Information on the Company

### *Messaging products*

In 2005 we launched Fixed SMS which allows fixed phone users to send text messages from SMS capable phones. We offer branded SMS capable cordless phones for sale in Telstra Shops and through Telstra dealers.

We also launched Telstra Online Text Buddy® which allows users to send text messages from computer desktops. At the same time we also launched Online SMS Desktop which is a business offering that provides a fully integrated SMS enabled desktop with business customers' existing email software.

### Data and Internet services

We provide new generation data and Internet services including:

- broadband and narrowband services for consumers and small and medium businesses through our ISP, BigPond®;
- business grade Internet solutions;
- IP Solutions; and
- domestic and international frame relay and ATM products.

We also provide data and specialised services, including ISDN, digital data services, voice grade dedicated lines, transaction/EFTPOS services and video and audio network services.

In relation to Internet services, one of our key focuses is on broadband. Our goal to provide broadband through our retail and wholesale channels to one million broadband SIOs by June 2005 was achieved more than a year ahead of schedule.

We offer a range of Internet products and packages under our BigPond® brand. Telstra BigPond® Home and Business offer dial-up modem and ISDN Internet services to residential and small and medium business customers across Australia. Telstra BigPond® Broadband provides broadband Internet services to consumer and small and medium business customers via hybrid fibre coaxial cable, satellite, ADSL and from August 2005 wireless technologies.

Telstra Internet Direct also provides business customers with high quality dedicated Internet access within Australia at access transmission rates up to one gigabyte per second (Gbps).

We also provide wholesale Internet access products for use by licensed carriers, ISPs and CSPs.

### *Other data services*

We offer other data services, in some cases with business partners, including:

- online games-based entertainment, sports information, video on demand and music services;
- collaboration services that provide audio, video and web-based conferencing (including the Conferlink® product range);
- ecommerce solutions including e-trading, e-payments, EFTPOS/ATM network services and straight-through processing services;
- Business DSL, that offers a broadband data service with symmetric data rates and business grade service levels with competitive pricing and extensive network coverage;
- Online Customer Management Facility (OCMF) providing a self-service capability for customers to manage user access to their IP networks;
- Connect IP solution range which is a standardised, end-to-end, IP based WAN offering that integrates network management and data connectivity with Customer Premises Equipment (CPE), allowing for seamless data transfer between customer sites;

## Information on the Company

- Digital Video Network (DVN) initiative allowing our media customers to share content such as news or sporting arena access over their DVN networks;
- IP Telephony, an open standard IP communications suite, which delivers hosted IP telephony and IP applications to our corporate customers; and
- Managed Wide Area Networks services (WANs) including design, CPE sales and installation, network establishment and maintenance.

***Online services***

In March 2000, we launched our online communications hub, telstra.com®. Since its creation, telstra.com® has grown substantially, with more than 1.452 million users as at 30 June 2005 (excluding BigPond®).

telstra.com® links customers with services and features including:

- information about our products and services;
- current Telstra corporate and investor relations information;
- online messaging applications such as web-based email and SMS;
- online product and service ordering and accounts viewing and payment; and
- a springboard to our ISP, BigPond®.

**Advertising and directories**

We are a leading provider of advertising and search services through our advertising business and wholly owned subsidiary, Sensis. Sensis delivers targeted, multi-channel solutions incorporating local advertising, classified advertising through our Trading Post Group, multi-channel search and a growing portfolio of business services to consumers, SMEs, corporations and Government. Although a mature market, the Yellow Pages® products have continued to deliver solid growth. This has been complemented by strong growth from White Pages®, non directories products and the successful integration of acquisitions in Australia.

In fiscal 2005, Sensis launched Sensis® 1234 (a premium operator assisted voice service). In July 2004, Sensis launched a new Internet search engine – sensis.com.au and shortly after the BidSmart® Pay for Performance search engine marketing system.

The Sensis Search portfolio provides an opportunity for our advertising customers to reach a new generation of search-orientated buyers:

- Sensis® 1234 is a voice service which provides a growing depth of business content from a vast array of Yellow Pages® and White Pages® products; and
- sensis.com.au is a benchmark online search engine which delivers global web content plus Australian directories, lifestyle and mapping content fully blended into the results.

The Business Services portfolio leverages our advertising and content management capabilities to create specific solutions for SMEs, Government and the corporate sector. Business Services is made up of three specific service portfolios – Business Information Services (incorporating the Sensis Direct Access contact data solution), Location and Navigation now incorporating Universal Publishers, (which delivers detailed street directory and geo-mapping functionality via a range of electronic channels) and our shareholding in Invizage Pty Ltd.

Sensis acquired 100% of the share capital of Universal Publishers Pty Ltd (Universal Publishers) on 20 December, 2004. Universal Publishers is a publisher of mapping and travel related products including street directories, guides, maps and road atlases through the Gregory's^ and UBD^ brands.

# Information on the Company

In June 2005, Sensis and Morgan and Banks Investments announced the launch of LinkMe®, an innovative online career networking site. LinkMe^ provides Sensis with an exciting, low risk opportunity to extend the multi-channel Advertising Network by entering a new classified vertical in a market-changing way. LinkMe® is Sensis' first foray into the online employment market.

**Wholesale services (including intercarrier services)**

In addition to providing products for resale, we provide a range of other products specifically tailored for wholesale customers. These include:

- interconnection services, including originating and terminating access to our fixed and mobile networks, preselection services and access to our network facilities such as ducts, towers and exchange space;
- domestic and international transmission services;
- broadband, IP backbone and traditional data services;
- mobile telecommunications services; and
- network design, construction, operations and maintenance services.

Both GSM and CDMA mobile products and services are offered to our wholesale customers.

We also manage and deliver a wide range of customer processes for wholesale customers. These include product and service provisioning, ordering and activation, billing, fault reporting and end user and product transfer. In addition, we provide a range of efficient web based business to business services to our customers.

We categorise revenue from the products and services we sell to wholesale customers according to the nature of the product or service. For example, we categorise operating revenue from interconnect charges as intercarrier services revenue. On the other hand, we categorise operating revenue from other resale services according to the product or service resold. For instance, basic access and local call revenue is recognised against basic access and local call products.

**Inbound calling products**

We offer inbound call services including:

- Telstra Freecall® 1800, a reverse-charge call service used widely by small and large businesses to extend market reach and attract sales;
- Priority® One3, a shared-cost service offering a six digit national number used by larger businesses as a front-door to contact centres and franchise operations for service calls;
- Priority® 1300 services, a shared-cost service offering a 10 digit number, similar to the Priority® One3 service, where a short-number format is not required;
- Contact centre enablement services, including network-based speech recognition and interactive voice response solutions, computer telephony integration, call routing services and speech recognition; and
- InfoCall® 190, a telephone premium-rate service where we bill the calling customer for both content and carriage on our bill and receive a fee from the content provider for these payment and carriage services.

# Information on the Company

### Solutions management

KAZ, our wholly owned subsidiary, currently operates as a standalone business servicing Government and large and medium sized business customers in Australian and Asia Pacific markets. KAZ combines with Telstra to service our business customers' IT needs, differentiating Telstra as the only communication company in Australia capable of providing end-to-end information and communications technology (ICT) services from within our own group of companies.

The business has been repositioned to focus on the ICT services market with Telstra providing the strong communications expertise, and KAZ to provide the IT expertise. We provide all or part of a business customer's IT and communications solutions and services covering:

- managed voice, data and mobility services: network based voice and data switching products including IP-based networks and IP Telephony as well as fleet management of mobile phone networks and new wireless based technologies;
- managed IT services: managed customer infrastructure (eg desktop and end user devices), and a range of solutions such as managed storage, security services, hosting and application development and support;
- IT outsourcing: incorporating a range of the above solutions and managing on behalf of the customer either on the customer's or our premises;
- business process outsourcing in areas such as superannuation administration, insurance policy processing and the automotive community; and
- solutions consulting, focusing on IP transformation, wireless enterprise and security.

### Other sales and services

The principal components of operating revenue we record in other sales and services relate to payphones, information and connection services, external construction, customer premises equipment, bundling subscription television and customnet and spectrum.

We are the leading provider of payphones in Australia. As at 30 June 2005, we operated approximately 32,500 public payphones. Our Universal Service Obligation requires us to make payphone services reasonably accessible throughout Australia including in non-metropolitan and rural areas. Approximately half of our public payphones are in these areas.

As part of our customer voice, data, mobile and service solutions, we provide customer premises equipment for rental or sale to our residential, consumer, business and Government customers. In relation to Telstra rental phones, modern new standard and 'calling number display' rental phones are available, making phone and phone features easier to use. In fiscal 2005 we improved our CPE offerings to the medium business market with the acquisition of Damovo (Australia) which now trades as Telstra Business Systems.

We provide information and connection services through a number of call centres in Australia and through the White Pages® *OnLine* and Yellow Pages® *OnLine* sites. In fiscal 2005, we responded to approximately 200 million calls through our call centres. We also provide voice recognition technology to allow the automation of approximately 2,500 of the most frequently requested business listings.

### Subscription television

We own 50% of FOXTEL, with Publishing & Broadcasting Ltd (PBL) and The News Corporation Limited (News Corporation) each owning 25%. The FOXTEL partners have committed, with very limited exceptions, to confine their involvement in the provision of subscription television services in Australia to participation in FOXTEL. PBL and News Corporation have made programming commitments to FOXTEL.

# Information on the Company

FOXTEL continues to be Australia's leading provider of subscription television services, with approximately 1.2 million subscribers (including subscribers resold by us and those receiving FOXTEL programming through Optus† television and TransAct). FOXTEL markets its services to more than 5 million homes, split reasonably equally between those homes passed by our hybrid fibre co-axial cable (HFC) and those marketable to via satellite distribution.

FOXTEL provides FOXTEL Digital^, offering customers access to a vastly expanded channel line-up of around 130 digital channels, superior picture and sound quality, a comprehensive and easy to use electronic program guide (EPG), interactive sports and news applications and FOXTEL Box Office^ (near video on demand).

In March 2005, FOXTEL launched the FOXTEL iQ^, a personal digital recorder (PDR) designed to change the way viewers watch television. The PDR is a next generation set top unit incorporating a 160Gb hard drive which enables subscribers to record two programs simultaneously, even while watching a previously recorded program.

In May 2005 FOXTEL announced an extension to its content wholesale relationship with Optus to facilitate Optus offering its subscribers access to the FOXTEL Digital^ suite of channels over the Optus HFC cable. In addition, FOXTEL announced an agency relationship with Optus for the distribution of FOXTEL in non-Optus HFC areas within the FOXTEL distribution area.

Under arrangements with the FOXTEL partners, FOXTEL may provide, in addition to subscription television services, a range of information and other services. FOXTEL currently only provides subscription television services.

We are the exclusive long-term supplier of cable distribution services for FOXTEL's cable subscription television services in our cabled areas and we receive a share of FOXTEL's cable subscription television revenues. We can independently, or through partnerships and alliances, provide a broad range of communications, data and information services to other parties using our broadband network.

FOXTEL has entered into various program supply arrangements, including some with minimum subscriber fee commitments. Refer to 'Operating and Financial Review and Prospects – Contractual obligations and commercial commitments' for further details regarding our exposure to these commitments.

We also resell Austar United Communications Limited (AUSTAR) subscription television services, which are eligible for inclusion in the Telstra Rewards Options plan. The bundling and reselling of both the FOXTEL and AUSTAR services broadens the range of telecommunication and entertainment services we offer to our customers. These arrangements allow us to provide a residential subscription television package to most areas in Australia regardless of geography.

A discussion of competition in the subscription television services market is contained in 'Competition and Regulation – Subscription television'.

## International investments

Our major international investments include:

- **CSL**, our wholly owned subsidiary which is one of Hong Kong's leading mobile operators with around 1.3 million customers, equating to approximately 32% of the value of Hong Kong's mobile market. CSL focuses on attracting and retaining high value customers and through its mobile brands, 1O1O and One2Free, CSL continues to offer its customers a highly targeted range of innovative mobile services;

# Information on the Company

- **TelstraClear**, our wholly owned subsidiary, is the second largest full service carrier in New Zealand. TelstraClear provides innovative voice, data, Internet, mobile resale, managed services and cable television products and services to the New Zealand market. New Zealand is a strategically important market for our trans-Tasman customers and this investment enables these important customers to receive many of the same end-to-end services that we provide in a seamless way; and
- **REACH**, a 50/50 joint venture with PCCW, which provides outsourcing services in support of Telstra's and PCCW's international voice and data services. REACH is also one of the world's top ten carriers of international voice traffic. REACH operates and maintains voice and data switching platforms, satellite earth stations and a network of over fifty submarine cable systems, together with associated landing rights, backhaul, operating licences and bilateral agreements in most international markets.

In April 2005 Telstra and PCCW, announced a number of improvements to the REACH operating model:

- allocation of dedicated components of REACH's international cable capacity to Telstra and PCCW;
- Telstra and PCCW each paid REACH US$157 million. In Telstra's case this was settled by way of a discharge of certain REACH liabilities under the Capacity Prepayment Agreement. Also, Telstra and PCCW each committed to fund a half share of REACH's committed capital expenditure (up to 2022), being about US$106 million each;
- REACH will manage allocated capacity on behalf of Telstra and PCCW and provide Telstra and PCCW with outsourcing and other services including data and voice;
- Telstra and PCCW will each pay REACH an outsourcing fee on a cost plus mark up basis, whilst satellite services will be purchased at market rates;
- REACH will continue its profitable third party voice and satellite business; and
- Telstra may fund and acquire further required cable capacity for management by REACH as part of the outsourcing arrangements.

We also have a number of smaller offshore investments and joint ventures, which include:

- a 35% equity interest in the satellite communications operator, Xantic B.V. (formerly Station 12 B.V.) that is headquartered in the Netherlands; and
- a 39.9% equity interest in Australia-Japan Cable Holdings Limited, a network cable provider headquartered in Bermuda.

## Capital Expenditures and Divestitures

For a discussion of the significant capital expenditures and divestitures we made in the preceding three-year period, refer to 'Operating and Financial Review and Prospects – Liquidity and capital resources'.

## Networks and systems

One of our major strengths in providing integrated telecommunications services is our extensive geographical coverage through both our fixed and mobile network infrastructure. This network and systems infrastructure underpin the carriage and termination of the majority of Australia's domestic and international voice and data telephony traffic.

This large, diverse network is monitored and supported through a largely centralised global operations centre, which has a fully tested recovery plan that enables network management to be transferred to an alternate location in the event of an unforeseen disaster. Ongoing substantial investment of both capital

# Information on the Company

and resources is required to ensure that we maintain this leading position from both a technology and industry position.

**Research and development**

Telstra reviews its project expenditure annually to determine its actual spend on research and development. Our reviews show that we had an estimated spend of A$148 million in fiscal 2005 on research and development. The expenditure was determined to be A$159 million in fiscal 2004 and A$240 million in fiscal 2003. For a detailed discussion of our research and development, refer to 'Operating and Financial Review and Prospects – Research and development'.

**Innovation Centres**

Innovation@Telstra was launched in October 2004, with the opening of Innovation Centres in North Ryde, Sydney and Melbourne's Docklands. Since then, thousands of people have visited the centres, gaining hands-on experience with Telstra products and services to make our business and home lives easier in the 21st Century. The centres are also used as a venue to fast-track innovation projects for Telstra ensuring that we develop customer-focussed solutions, which get to market in a speedy manner.

In addition to customer visits, the Innovation Centres have also delivered a number of key projects via the Innovation PODs - a dedicated project floor focussing on accelerating solutions to market.

Some of these projects include:

**The Digital Home:** The strategy for home-based IP services delivering communication, entertainment, information and storage as well as security and automation services.

**Community Information Warning System:** A proactive community information, communication and warning system to save lives, reduce losses and speed recovery in the event of natural disasters, accidents or acts of terrorism.

**Remote Working:** A comprehensive solution for remote access to corporate customers' private data networks.

**Transmission infrastructure**

Our national transmission infrastructure consists of both terrestrial and non-terrestrial transmission systems. Our domestic terrestrial systems are almost exclusively digital and use approximately 4 million kilometres of optical fibre and more than 2,300 digital radio systems. Our major transmission routes incorporate Synchronous Digital Hierarchy (SDH) technology.

Throughout the year, work has continued on extending the benefits of self-healing SDH transmission out to the fringes of the network in metropolitan and regional areas. In total, approximately 20,000 additional customers now benefit directly from improved transmission survivability.

Our international switching and transmission requirements are provided by REACH, which owns international gateway switches in Sydney and an expanding network of switches across Asia, North America and Europe to augment its state-of-the-art global data/IP system. REACH uses satellite communication systems to supplement international traffic capacity where undersea cables are not feasible and to provide route diversity and circuit redundancy, as well as specialist satellite-based applications. REACH owns satellite earth stations in Australia and Hong Kong, including the largest satellite teleport in Asia.

# Information on the Company

### Public Switched Telephone Network (PSTN)

Australia’s geographic characteristics provide unique challenges for the provision of nationwide digital PSTN coverage. These challenges are being overcome by the innovative application of a range of modern technologies. Over 300 major digital switching nodes are interconnected by state-of-the-art transmission systems and handle traffic from customers connected to more than 10,000 access sites. A combination of copper, fibre optic, radio and satellite technologies is used to achieve end-to-end connections. Access to the world is achieved through REACH’s international gateway switches and our intelligent network platforms provide advanced services including toll-free and calling card products.

We have deployed CDMA-based wireless local loop technology in regional Australia as part of our contract with the Commonwealth Government to improve communications in extended zones. Further deployment of this technology is planned as part of the recovery of older radio concentrator technology. It is also planned for selected use to provide telephony access for customers to whom traditional copper pair access is inefficient.

The PSTN supports voice, facsimile, Internet and data products. Total call minutes handled by the PSTN is now showing a slight decline as data traffic moves to broadband access. The combination of new broadband access services and growth in dial-up Internet usage, messaging services and mobile telephony is leading to convergence of voice and data in the longer term. This will provide a solid base for seamless transition to future convergent service provision.

Our network supports a range of switch features which facilitate voice calls. These include products like Homeline® Features such as Call Waiting, Call Return, Abbreviated Dialling and Virtual Private Networks (VPN). New types of telephones and customer premises equipment which make these features more accessible and easy to use are continually entering the market.

The PSTN also supports many operator assisted service products such as directory assistance and CallConnect. We are seeking to enhance these services by automating them with voice recognition technology.

### Fibre to the Premises (FTTP)

FTTP is a next-generation access infrastructure technology that can deliver telephony, broadband data, video and digital subscription television services, to customer premises on an optical fibre platform. Fibre to the Premises is expected to play a pivotal role in Telstra's customer access network, along with copper, wireless and satellite technologies.

In June 2004, Telstra commenced an initial pilot of FTTP in two Queensland sites. The FTTP pilot is now successfully providing services to a number of residential homes, and continues to provide Telstra with insight into the ongoing effectiveness of FTTP as an access technology of choice.

We have also been trialling Voice over Broadband (VoBB). This solution will be provided as a second line solution offering a range of features and functionality for users with a broadband connection. During fiscal 2005, a VoBB network trial was completed with 150 of our employees in Melbourne.

### Integrated Services Digital Network (ISDN)

ISDN is a flexible, switched digital network. The integrated nature of this network refers to the fact that ISDN can support many applications at the same time while using a single access point to the network. The ISDN network supports traditional telephony as well as various data applications such as videoconferencing, Internet access and EFTPOS.

# Information on the Company

The ISDN network is available to approximately 96% of the Australian population. ISDN provides an end-to-end digital connection that allows us to deliver minimum 64kbps connections to customers.

**Intelligent Network (IN) platforms**

We operate a number of IN platforms that support a range of advanced services across fixed, mobile and messaging services including:

- inbound services such as Telstra Freecall® 1800, Priority® One3, Priority® 1300 and InfoCall® 190;
- Telstra prepaid mobile, Pre-paid Plus;
- calling cards (Telecard®);
- prepaid cards (Phoneaway®, Say G'day®);
- information services numbers;
- number portability;
- mobile VPN, mobile voicemail;
- advanced network routing; and
- screening functions.

Our inbound services are important to our major business customers because they support their call centre and customer service operations.

**Data networks**

We operate a number of data networks including a:

- Switched Data Network (SDN);
- National Transaction Switching Network; and
- Digital Data Network (DDN);

Our SDN comprises approximately 730 switches linked to access multiplexers at more than 120 sites around Australia. The SDN provides:

- public packet switching data services suitable for a wide range of data applications;
- site-to-site and multi-site WAN connectivity;
- national coverage for frame-relay data services from 64kbps up to 45Mbps (subject to available transmission capacity);
- national coverage for ATM data services, supporting access rates from 2Mbps to 622Mbps (subject to available transmission capacity); and
- national coverage for Business DSL data services, supporting access rates from 64kbps to 2Mbps (subject to available transmission capacity).

SDN is also the backbone for numerous IP WAN services, supporting a range of access types from the fixed ATM and frame services for domestic and global use to Dynamic Dial, ADSL, wireless services and value-added features including firewalls, hosting, Messenger, IP Voice and IP Video.

Our retail customers use ATM and frame relay data services on the SDN to build wide-area corporate data networks. Our wholesale customers use the SDN as a key element of their own retail offerings.

Our National Transaction Switching Network is suitable for electronic funds transfer and inventory applications. This network provides dedicated and dial-up access in a secure environment, suitable for transmitting transactions.

# Information on the Company

Our DDN, with its fully integrated management system, provides dedicated secure site-to-site transmission at speeds ranging from 1200bps up to 2Mbps. This network has extensive coverage, with more than 2,500 points of presence nationally across Australia for both Telstra retail DDS and Telstra Wholesale Data Access Radial (DAR) products.

In addition, the DDN is the underlying access infrastructure for our Accelerated Frame Relay product using our large network reach over multiple access technologies such as G.Shdsl, HDSL and optic fibre to enable customer access into the SDN core network. DDN also supports the declared wholesale product of Data Access Radial, which supplies the access for carriers to enable their customers to connect to their own retail offerings.

**Internet Protocol (IP) networks**

We operate a national Internet backbone network. It is a fully IP-routed network, which provides the backbone for all of our Telstra Internet Direct services and all Telstra BigPond® Internet offerings, as well as Telstra Wholesale's Internet products. Our Internet backbone network connects to the rest of the Internet via the international links provided by REACH and connects domestically via peering links with peer ISPs.

We operate two major Internet data centres, one in Melbourne and one in Sydney. The computer server infrastructure in these centres controls access to the network and provides applications including email, news, chat, web hosting and games. The server infrastructure supports real time activation of customers and also provides billing functionality, service monitoring and surveillance. Caching servers are deployed to store and serve often requested Internet content so that customers receive faster web page delivery and we are able to contain our Internet traffic costs.

We have one platform that supports wholesale and retail Internet products. This has been used to provide a Telstra BigPond® Home product with universal local call access across Australia. Telstra BigPond® Home is now available throughout Australia with dial-up access at the cost of a local call.

We deliver our IP Metropolitan Area Network (MAN) and Telstra Ethernet MAN services through an MPLS network that has ethernet switches located in customer buildings and interconnected by a high-speed network. IP MAN plus IP WAN together form the network to deploy our IP Solutions products. We are offering a Government IP solution which provides a fibre based IP network for use by Government agencies in metropolitan and regional locations, as well as accelerating the provision of fibre based wideband services by non-Government customers.

We have also extended the core, carrier grade IP network known as the Routed Data Network (RDN) to sites in metropolitan and some regional areas. The RDN supports the delivery of retail and wholesale ethernet based products nationally.

**Broadband network**

We deliver broadband capability through a variety of technologies using cable modem, ADSL and satellite services. Our HFC broadband network passes approximately 2.7 million homes and approximately 73% of the network is underground. The optic fibre component of this broadband network consists of two forward and one return path fibres, with the co-axial component serving an average of 900 customers each.

The cable network is designed to provide two-way transmission for interactive services and high-speed data transfer up to 10Mbps with an average speed of 6Mbps typical. ADSL is a broadband access technology using existing PSTN access infrastructure capable of speeds up to 7.8Mbps depending on distance from exchange and line condition. Current products offer speeds up to 1.5Mbps downstream and up to 256kbps upstream or 512kbps both ways. Although not yet commercially deployed, ADSL2 + capability has been introduced into 270 exchanges and offers up to 24Mbps downstream and 1Mbps upstream.

## Information on the Company

We have three fast broadband service options available to customers in ADSL enabled areas in Australia:

- an Internet service for residential customers that allows customers to use the Internet through their existing telephone lines without tying up the phone line or needing an additional line;
- an Internet service for companies to provide their staff, offices or branches with remote access capability to the corporate network; and
- a service for ISPs to provide their customers with ADSL Internet access.

Since August 2000, we have been rolling out our broadband services and we achieved our target coverage for fiscal 2005 of approximately 1,700 ADSL enabled exchanges.

We also offer satellite broadband services via both a two way satellite service and a satellite download/dial-up backchannel in areas of Australia for customers who are unable to access broadband via cable or ADSL.

We are a registered provider under the Australian Government's Higher Bandwidth Incentive Scheme (HiBIS). This scheme aims to increase the availability of high bandwidth services throughout rural and regional Australia at prices that are broadly comparable with metropolitan areas. We have used the incentive to reduce the threshold levels on its ADSL Demand Register, making it easier for smaller communities to trigger ADSL investment. Between the period April 2004 when the scheme commenced, and June 2005, we provided ADSL to almost 600 rural and regional exchanges with the assistance of HiBIS funds. For more remote customers, we used the HiBIS subsidy to reduce the prices of BigPond® 2-way Satellite and Broadband Regional Connect, a combination of an ISDN service and a 1-way satellite uplink.

**Mobile telecommunications networks**

We own and operate a number of networks for the provision of mobile telephone services that together cover more than 98% of the Australian population. We serve more than 8 million SIOs with these networks. Through CSL we also operate mobile services in Hong Kong.

In Australia, our GSM digital network operates in the 900MHz and 1800MHz spectrum bands. As at 30 June 2005, our GSM digital network in Australia had approximately 4,000 base stations nationally. We are continuing to expand the capacity and coverage of the GSM network, with more than 280 new base stations established in fiscal 2005.

The GPRS service is available across our GSM network and provides 'always on' data access to WAP and Internet information services, as well as access to corporate customers' LANs and intranets.

Our 3GSM service operates in the 2100Mhz spectrum band. At launch during 2005 our 3GSM consisted of approximately 2,100 base stations nationally. Video and higher speed 'always on' packet data access is available across our 3GSM network footprint.

Our second digital mobile telecommunications network in Australia is based on CDMA technology, with coverage more than double the area of the GSM network. We are predominantly developing new regional areas of coverage in this technology. It operates in the 800MHz band that our closed analogue network used previously. As at 30 June 2005, our CDMA digital network in Australia had approximately 3,000 base stations nationally. We are continuing to expand the capacity and coverage of the CDMA network, with more than 230 new base stations established in fiscal 2005.

Enhancement of our CDMA network with 1xRTT commenced in fiscal 2003 and focussed on all capital cities. The final stage of the transition to 1xRTT began in February 2004 and has now been completed. A limited rollout of the next generation mobile data utilising EVDO has been completed in all capital cities and some regional centres. Further expansion of this technology is currently being built in Sydney and other areas are being scoped.

# Information on the Company

### Electromagnetic energy (EME)

We rely on the expert advice of national and international health authorities such as the Australian Radiation Protection and Nuclear Safety Agency (ARPANSA) and the World Health Organisation (WHO) for overall assessments of health and safety impacts. The consensus is that there is no substantiated scientific evidence of health effects from the EME generated by radio frequency technology, including mobile phones and base stations, when used in accordance with applicable standards.

Certain reports have suggested that EME emissions from mobile phone base stations and radio communications facilities (including handsets) may have adverse health consequences for users and the community. We are committed to being open and transparent on all issues relating to EME emissions. We comply with all relevant radio frequency standards and have comprehensive policies and procedures to ensure the health and safety of the community and our employees.

Telstra Research Laboratories ensure that we have accurate and scientifically substantiated information and contribute to the national and international EME research program. In the last 11 years we have invested more than A$10 million in this program.

An area of industry leadership is the development of base station EME software that calculates environmental emission levels in a matter of seconds. Our widely acclaimed RF-MAP™ software enables operators, local authorities and community groups to assess the environmental impacts of mobile phone base stations and confirm compliance with safety standards. We have given copies of our RF-MAP™ software to national and international health authorities as well as community and Government organisations, reflecting our commitment to sharing expertise and providing the community with easy to use solutions.

Australian carriers, through the Mobile Carriers Forum, are developing a site management process to help ensure compliance with the Australian Communications Authority (ACA) electromagnetic radiation framework and the Australian Communications Industry Forum (ACIF) code of practice for radio communications infrastructure deployment. We developed tools such as national site archive and National Antenna rooftop database which are being adopted by the Mobiles Carrier Forum.

### Information processes and systems

We have a range of information processes and systems to support our delivery of products and services. We intend to increase the benefits of our offerings to customers by:

- introducing new products to the market faster;
- further integrating our customer access technology and systems across channels; and
- reducing our overall IT costs.

We have recently invested and will continue to invest in many new systems and processes in the following seven principal areas:

- sales and marketing;
- customer ordering and provisioning;
- online access for customers;
- billing and credit management;
- service assurance;
- workforce management; and
- back office processes.

# Information on the Company

We are focussed on rationalising and simplifying the delivery processes across Telstra. Together with our IT service providers, we will focus on driving efficiency and adaptability across our delivery systems.

In April 2005 we established Business Process Owners who have company wide accountability for their respective processes. We aim to continue significant improvements in our processes which will contribute to reduced cycle times, increased revenues and importantly, improved customer experience.

### Information technology

In response to increased competitive pressures in Australia and internationally, we source in the global market innovative, world-class solutions for the provision of application development and maintenance services. This includes the development of new software programs and the enhancement and ongoing maintenance of existing software programs.

We are partnering with world class IT providers to deliver:

- improved quality to a globally competitive standard;
- improved cycle times for new products and services;
- improved efficiency and lower prices; and
- access to new technologies.

## Property, plant and equipment

### Overview

A large part of our network is constructed on land occupied under our statutory powers and immunities. We also own and occupy land that includes strategic sites, such as the properties on which our telephone exchanges are located. We own 5,067 freehold sites and occupy 8,305 sites on a leasehold or other basis. Most of our sites are related directly to our telecommunications operations and are used for housing network equipment of various types, such as telephone exchanges, transmission stations, microwave radio equipment and mobile radio repeater equipment. Some of our operational sites are on leased land or land that we have access to by statutory right or other formal or informal arrangement. In addition to our operational sites, we own or lease a range of properties used for office accommodation, storage and other miscellaneous purposes which are discussed in 'Operating and Financial Review and Prospects - Contractual obligations and commercial commitments'.

### Land access powers and immunities

The land access powers and immunities conferred on carriers by the Telecommunications Act 1997 (Cwth) (Telecommunications Act) are limited to those inspections, maintenance and installation activities that will have a low impact on the surrounding environment. For activities not covered by the land access powers and immunities regime, we must obtain all necessary consents, including the consent of the relevant town planning authority as well as from the owner of the land, before network construction activities may commence. Where the construction activities are to occur on land where native title exists, the native title claimants and holders may also need to be involved. Obtaining these consents may cause delay to the commencement of construction.

In some circumstances where we rely on the land access powers and immunities conferred by the Telecommunications Act to carry out construction activities or where native title exists, compensation may be claimed against us.

# Information on the Company

### Environmental issues

Environmental aspects covering the handling and storage of dangerous goods, noise from fixed plant, visual amenity and disposal of waste (including obsolete and decommissioned equipment) are required to be managed as part of operating and maintaining plant and equipment on occupied sites. We minimise the potential risks associated with these environmental aspects through various control procedures. Incident processes are in place to minimise the potential impacts of environmental incidents. Each decommissioned plant is screened for hazardous substances such as polychlorinatedbiphenyls (PCBs) and chloroflurocarbons (CFCs) prior to recycling and hazardous materials are disposed of in compliance with regulatory requirements. Sites to be divested undergo environmental assessment and, if appropriate, remediation, prior to sale.

There are no current significant environmental issues that impede the utilisation or integrity of our network operation.

# Competition and Regulation

## Competition

### Overview

Competition in Australia's telecommunications market began in 1989 when competitors began to provide a limited number of services. In 1991, competition increased with the decision to establish a carrier duopoly and open resale of Telstra's services, particularly national long distance and international telephone services. Competition intensified in 1992 when Optus, now SingTel Optus Pty Limited (Optus), won the second carrier licence enabling it to offer unrestricted local, national long distance, analogue mobile and international telephone services. We started offering digital mobile telephone services over our own network in 1993. In the same year, Optus and Vodafone Holdings (Australia) Pty Limited (Vodafone) began offering those services over their own networks.

On 1 July 1997, the Commonwealth Government introduced the current regulatory regime which provides for open competition in Australia's telecommunications industry. Since then, there has been a significant increase in the number of CSPs that have entered the Australian telecommunications market. As at 30 June 2005, we supplied services to more than 600 wholesale customers that compete in the retail telecommunications market.

From a position of originally being the sole provider of telecommunications products and services in Australia, inevitably, competition has reduced our market share. However, competition has also contributed to growth in the overall telecommunication services market. We expect both these trends to continue but at lower rates.

As at 30 June 2005, we estimate our retail market shares in the products and services we provide to be as follows: basic access services: 73%; local calls: 73%; domestic long distance minutes: 62%; international long distance minutes: 51%; mobile services: 45%; Internet services (narrowband): 28%; Internet services (broadband): 41%; data revenue: 62% (excluding ISDN but including some wholesale revenues); subscription television services (FOXTEL): 60%; and Sensis print advertising expenditure (main media): 13%.

We are permitted to compete in all telecommunications markets throughout Australia. Our competitors are also permitted to compete in all of these markets. As convergence becomes more prominent, our competitors may seek to take advantage of their position in one market to enter or improve their position in another market.

### Access and local calls

We currently face infrastructure competition in basic access and local call services in the central business districts of the major capital cities and major metropolitan areas. Many of these infrastructure competitors have access networks which compete directly with us for both business and residential customers. Our main facilities-based competitors are Optus (fixed and mobile), Vodafone (mobile), AAPT Limited (AAPT) (fixed) and Primus Telecommunications (Australia) Pty Limited (Primus) (fixed). These carriers and others have established dedicated connections with large business customers, mainly in central business districts. Dedicated connections allow a competitor to direct a business' telecommunications traffic to their own networks including local, long distance and international calls and data transmission. The availability of local number portability has contributed to the development of facilities-based competition in these markets. We also face increasing competition from fixed to mobile and Voice over Internet Protocol (VoIP) calls.

# Competition and Regulation

### National Long Distance and International Telephone Services

Competition has significantly eroded our market share for national long distance and international telephone services. Our competitors usually own their own switches and acquire the PSTN originating and terminating access from Telstra. To provide the national long distance and international telephone services, they also need to own or lease transmission capacity.

We must provide our customers with call-by-call selection or ‘override’ dialling and default choice or ‘preselection’ in respect of national long distance, international calls and fixed-to-mobile calls, all of which further assist other CSPs to compete. See ‘Competition and Regulation – Regulation – Preselection and override codes’ for a discussion of regulatory requirements for preselection.

The PSTN originating and terminating access and the wholesale transmission capacity services are important for facilities-based provision of national long distance and international telephony services. The charges of these wholesale products are input costs of the competitors and therefore have an impact on their retail offerings.

The regulatory processes provide a framework to determine the price terms and conditions of these services. Competition is strong in the wholesale provision of transmission services. The price is falling as new competitors enter the wholesale market. The ACCC will review the rest of the wholesale domestic transmission capacity by March 2009.

### Mobile telecommunications services

The mobile telecommunications market is one of the most competitive telecommunications markets in Australia and we estimate that market penetration as at 30 June 2005 was approximately 90%. As this level of market saturation increases, we expect the rate of further market penetration to slow for all carriers.

The composition of new subscribers is also changing as growth in subscriber acquisitions is driven more by pre-paid services, rather than the traditional post-paid contract customers. Increasingly, mobile service providers are looking to future growth in revenue from data usage by existing subscribers. There is evidence of strong growth in data usage which is currently driven by the popularity of SMS. Agreement between carriers for inter-carrier SMS between GSM and CDMA networks has facilitated this growth.

### Data services

The Australian data market is intensely competitive, with a number of service providers in a range of categories from network, ISPs, international and Managed Service Providers (MSPs) offering a range of domestic and international services. Competitors are typically classified as resale or infrastructure competitors and may provide fixed line and wireless data solutions.

Customers are increasingly taking up new growth data services based on DSL, Ethernet or IP-based solutions. Competition is intense in these growth areas, particularly across niche product solutions and specific geographic areas. Several DSL network providers are offering DSL based VPN services as an alternative to frame relay or leased line data connections. Others are also offering Voice over DSL (VoDSL), with a view to offering integrated voice and data bundles.

## Competition and Regulation

### Internet access services

For Internet access services, competition is based on a number of features including quality of service, price, speed and availability of local call access and associated information or transaction services. The ISP market in Australia is diverse and highly competitive, with approximately 680 competing retail service providers.

We provide both dial-up and broadband Internet access services. Broadband services are provided to end-users by Telstra BigPond® using ADSL, cable, wireless and satellite platforms. Telstra Wholesale provides industry participants with a variety of broadband offerings including DSL Layer 3, DSL Layer 2 and Virtual ISP Broadband. We also offer an ISDN Internet access service as an alternative to standard PSTN dial-up to deliver faster Internet speeds for both retail and wholesale customers.

### Online services

Our online, content and web hosting services are subject to a high level of competition from domestic and international competitors. We seek to differentiate ourselves through a variety of factors including brand recognition and the entertainment, educational and commercial value of our content. We are meeting customer demand by offering our own content and forging alliances with content providers.

We provide services under a range of brands including telstra.com®, BigPond®, Yellow Pages®, White Pages®, Whereis®, CitySearch^ and sensis.com.au.

### Wholesale services

Telstra Wholesale has more than 600 customers, including approximately 470 ISPs, and operates in a market with about 34 wholesale competitors. Telstra Wholesale is focused on the delivery of communication services to intermediaries operating in Australia and offers around 40 wholesale-only products for our customers such as PSTN interconnection, data access radial, ViSP and a variety of ADSL products.

### Subscription television

The subscription television services market is competitive. FOXTEL (of which we own 50%) is the leading subscription television provider in Australia, with in excess of 1 million subscribers (aggregating FOXTEL's direct subscribers and subscribers receiving resold FOXTEL services via Telstra and others) as at 30 June 2005. In addition, FOXTEL also supplies its programming to Optus and TransACT on a wholesale basis, with those two companies utilising that programming to supply subscription television services to more than 155,000 subscribers in aggregate. Collectively, FOXTEL is now seen in approximately 1.2 million households.

FOXTEL is well positioned to compete on the basis of its brand and diverse program offerings delivered over both digital and analogue cable (via Telstra) and digital satellite. In fiscal 2005, FOXTEL grew its subscribers by more than 13%.

FOXTEL and Optus television are the main providers of subscription television services over cable in largely overlapping areas. Optus is expected to launch a digital subscription television service during fiscal 2006. FOXTEL also provides digital satellite coverage to approximately 2.5 million homes not passed by our cable network.

AUSTAR distributes subscription television through digital satellite systems in regional areas and has similar programming to FOXTEL. FOXTEL and AUSTAR compete only in limited areas. While there are no restrictions on FOXTEL entering the AUSTAR territory, many of the program rights held by FOXTEL do not permit it to broadcast that content into the AUSTAR territory. Also, FOXTEL has licensed some programming to AUSTAR on an exclusive basis in relation to most of the AUSTAR territory. Other subscription television operators offer limited services.

# Competition and Regulation

Subscription television providers compete with free-to-air television operators and are prevented by law from holding exclusive broadcast rights to most major sports programs. Competition is currently based on a number of factors including breadth of programming, brand, price, marketing, service support and geographic scope of service delivery.

The obligation to provide a digital cable subscription television access service was subject to either Telstra launching such a service commercially or the ACCC granting Telstra and FOXTEL exemptions from the operation of Part XIC of the Trade Practices Act 1974 (Cwth) (TPA) in relation to that service. The ACCC's decision to grant these exemption orders were taken on appeal to the Australian Competition Tribunal. The appeal was upheld, and in September 2004 the Tribunal set aside the ACCC's original decision to grant exemption orders and ruled that no exemption orders should be granted to Telstra and FOXTEL. Telstra commenced the commercial supply of digital cable subscription television carriage services to FOXTEL in March 2004. Although there is no exemption order in Telstra's favour, Telstra offers to supply digital cable subscription television carriage services commercially to access seekers pursuant to the terms of the undertaking accepted by the ACCC in 2003.

### Advertising, Directories and Information Services

Our White Pages® and Yellow Pages® directories, classifieds business and related products (print, online, voice and wireless services ) are key advertising and contact information channels for Governments and businesses, in particular SMEs across Australia. As such, we operate within the highly competitive Australian advertising market, competing with a range of other domestic and international advertising businesses, search engines, local newspapers and direct marketing companies which also target a similar customer base.

Competing directory providers have access to CSP subscriber contact details from the Integrated Public Number Database (IPND) which we maintain as a requirement of our carrier licence.

### Payphones

In our payphones business, we are seeing increasing competition due to new market entrants, calling card operators and indirect competition from increased mobile telephone use.

## Regulation

### Overview

Some of the major features of the Australian telecommunications regulatory regime are:

- industry specific competition regulation;
- any to any connectivity;
- extensive industry specific consumer protection regulation;
- industry codes and standards under a self-regulatory regime;
- no limits on the number of carriers;
- CSPs with many of the same access rights and obligations as carriers; and
- limited carrier land access rights and statutory immunities.

The Government has announced a review of the regulatory regime of the telecommunications sector ahead of any further privatisation of Telstra. Further, as part of this review, the Government is considering whether some form of operational separation would be appropriate for Telstra to ensure transparency. This process and the review of the regulatory regime have commenced, however it is yet to be completed.

# Competition and Regulation

## Principal industry regulators

The Communications Minister is primarily responsible for telecommunications industry policy and legislation. The Communications Minister can make rules in connection with the implementation and operation of certain aspects of the regulatory regime and, at his or her discretion, impose or vary the conditions of a carrier licence. In addition, the Communications Minister has the power under section 159 of the Telecommunications (Consumer Protection and Service Standards) Act 1999 (Cwth) to give binding directions to us to take specified action towards ensuring that we comply with that Act. This Ministerial direction power applies in addition to the Ministerial power in Part 3 of the Telstra Act to give such directions in relation to the exercise of powers by us as appear to the Minister to be necessary in the public interest.

The ACCC administers the TPA which regulates competition generally and includes specific provisions governing the telecommunications industry. The ACCC administers the telecommunications access regime, provisions for controlling anti-competitive conduct and Telstra retail price control arrangements.

As of 1 July 2005 the ACA and the ABA merged to form the Australian Communications and Media Authority (ACMA). The Government has decided that there will be no changes to the current functions carried out by the ACA or the ABA. The ACMA will be responsible for regulating telecommunications, broadcasting, online content and radiocommunications. From 1 July 2005, all references to the ACA in this document should be read as referring to the ACMA.

The ACA is responsible for reporting on telecommunications industry performance and regulating the non-competition aspects of the telecommunications industry under the Telecommunications Act and the Telecommunications (Consumer Protection and Service Standards) Act including:

- carrier licensing;
- technical regulation;
- quality of service;
- the customer service guarantee;
- priority assistance;
- network reliability framework;
- preselection, numbering and number portability;
- the universal service obligation;
- the digital data service obligation;
- spectrum management; and
- industry codes and standards.

The ACA may give written directions to carriers, CSPs and content service providers requiring them to comply with various provisions of the Telecommunications Act, the Telecommunications (Consumer Protection and Service Standards) Act, their licence conditions and registered industry codes. Breach of such a direction is subject to a penalty of up to A$10 million.

The ACCC and the ACA are independent statutory agencies. The ACCC is not generally subject to the control or direction of the Communications Minister or the Commonwealth. The Communications Minister has a power of direction in relation to the ACA. However, both the ACCC and the ACA can take action regarding the regulation of the telecommunications industry without the prior approval or knowledge of the Communications Minister or the Commonwealth.

The Telecommunications Industry Ombudsman (TIO) is an industry-funded body established to investigate and resolve retail customer complaints about telecommunications services and carrier land access disputes. Participation is mandatory for all carriers and most CSPs unless exempted by the ACA.

# Competition and Regulation

### The industry also self-regulates through codes and standards

Bodies that represent one or more sections of the industry, such as the ACIF, may develop industry codes governing activities of carriers, CSPs and other industry participants. These activities mainly relate to matters affecting:

- consumers;
- inter-carrier operations;
- interconnection and performance of networks;
- radio;
- environmental issues; and
- customer equipment and cabling.

The ACA may register such codes under the Telecommunications Act, direct industry participants to comply with a registered code and, in the absence of a registered code, set mandatory industry standards. If a carrier or CSP does not comply, it may be subject to a penalty of up to A$250,000. The ACIF also has compliance mechanisms for breach by an industry participant of an ACIF code to which the participant has agreed, which include non-monetary ‘public censure’ sanctions.

The codes registered under Part 6 of the Telecommunications Act with the ACA as at 18 August 2005 relate to:

- the handling of life threatening and unwelcome calls;
- call charging and billing accuracy;
- end-to-end network performance;
- preselection;
- commercial churn;
- calling number display;
- complaint handling;
- customer information on prices, terms and conditions;
- billing;
- credit management;
- customer transfer;
- local and mobile number portability;
- unconditioned local loop service network deployment rules;
- IPND, data provider, data user and IPND manager;
- emergency call services;
- deployment of radiocommunications infrastructure;
- cabling requirements for business;
- priority assistance for life threatening medical conditions;
- customer and network fault management; and
- SMS.

### Carriers, carriage service providers and content service providers

We are a carrier, CSP and a content service provider.

A carrier is any person holding a carrier licence. In general, the owner of network infrastructure must not use the infrastructure to supply telecommunications services to the public unless it holds a carrier licence. A CSP is a person who supplies a telecommunications service to the public using network infrastructure owned by a carrier. A content service provider is a person who uses a telecommunications service to supply to the public a content service, such as a broadcasting service or an online information or entertainment service.

# Competition and Regulation

## Competition regulation

### *Competition rule*

In addition to the general requirements of trade practices law, a carrier or CSP must not engage in anti-competitive conduct in breach of the competition rule. A carrier or CSP may be in breach of the competition rule if it:

- contravenes general trade practices rules relating to anti-competitive conduct in respect of a telecommunications market; or
- has a substantial degree of market power and takes advantage of that power with the effect or likely effect of substantially lessening competition in any telecommunications market, taking into account other conduct if necessary.

The ACCC can issue a Part A competition notice if it has reason to believe that a carrier or CSP has contravened the competition rule. A Part A competition notice need not describe conduct in very specific terms but may instead describe the general kind of conduct which the ACCC believes is in breach of the competition rule. Any repetition of the conduct while the competition notice is in force can lead to penalties or damages being awarded against the carrier or CSP.

The ACCC can also issue a Part B competition notice. This Part B notice, which the ACCC may issue simultaneously with or after a Part A notice, will be more detailed than the Part A notice. The sole function of a Part B notice is its evidentiary effect. It is presumptive evidence of the information in it and can be used in court proceedings against the carrier or CSP for penalties or damages.

To issue a competition notice (Part A or Part B), the ACCC need only have a reason to believe that there is a breach of the competition rule rather than being affirmatively satisfied of a breach of the competition rule after full investigation.

Any person (including a carrier's or CSP's competitors) may apply at any time to the Federal Court for an injunction to restrain anti-competitive conduct, whether or not a competition notice has been issued.

A carrier or CSP may be liable to pay penalties of up to A$10 million plus A$1 million per day of contravention, and for compensatory damages to affected third parties, if:

- it continues to engage in conduct the subject of a competition notice after the notice comes into effect; and
- the Federal Court finds that the conduct is in breach of the competition rule.

No final decision in relation to a competition notice has yet been handed down by a court.

If the ACCC issues a competition notice, it may also give a carrier or CSP a written notice advising it of the action the ACCC believes should be taken to ensure that the carrier or CSP does not continue to engage in the kind of conduct dealt with in a Part A competition notice. An advisory notice can be issued at any time. While such a written notice from the ACCC is of an advisory nature only, in practical terms there may be significant pressure on a carrier or CSP to comply with the notice given the potential breadth and ambiguity of a Part A competition notice and the ability of the ACCC to revoke a Part A competition notice if the carrier or CSP complies with the advisory notice. Also, a court may have regard to the ACCC's opinion in determining whether a carrier or CSP is liable for penalties or damages if the court finds it to have been in breach of the competition rule.

A competition notice relating to changes to BigPond® Broadband pricing was issued against Telstra in March 2004. The competition notice was withdrawn following agreement between the ACCC and Telstra in February 2005.

## Competition and Regulation

### *Information gathering powers*

The ACCC may seek information from carriers or CSPs with substantial market power in the telecommunications industry concerning charges for products and services, including in Telstra's case only, charges for basic carriage services, subject to a right of appeal to the Australian Competition Tribunal. The ACCC may publish information concerning charges and services if it is satisfied that there would be a net public benefit in doing so and has a further general power to obtain information in relation to designated telecommunications matters.

### *Record-keeping rules*

The ACCC has in place financial record-keeping rules. These accounting rules require detailed three or six-monthly reporting to the ACCC of non-public cost and revenue information in relation to our wholesale and retail services.

The ACCC will be able to refer to this information on our costs and revenues in its market conduct and access investigations. Similar accounting rules apply to both Optus and Vodafone. AAPT and Primus are required to comply with the same rules but only in relation to retail services.

### *Accounting Separation*

In April 2002, the Communications Minister announced that the Commonwealth Government required accounting separation of our wholesale and retail arrangements in order to ensure our wholesale arm treats all retail providers in an equitable fashion.

On 19 June 2003, the Communications Minister issued the final Accounting Separation Direction to the ACCC requiring it to issue record keeping rules to Telstra giving effect to that direction. One requirement of the direction is for Telstra to update its regulatory accounting records to produce both historic and current cost accounts, which has and continues to impose some resource costs on us. Preparation of the regulatory accounts for the core PSTN services of PSTN interconnection, local call resale and the unconditioned local loop will provide a basis for comparison in relation to any existing regulated prices for these products. We have already produced two interim reports but we are still working towards finalising these reports. The interim reports are based on a range of assumptions, hence the results should be treated with caution.

An additional requirement under the accounting separation rules is for Telstra to prepare and for the ACCC to publish imputation test results for various PSTN services including basic access, locals calls, national long distance, international long distance and fixed to mobile services. An imputation test measures whether an efficient competitor of Telstra can compete against our retail product offering, based on our retail price and an assessment of the efficient wholesale and retail costs to the competitor of providing the service. In the context of the accounting separation obligations, these costs are determined by the information in our regulatory accounts.

The ACCC is also required to publish a series of metrics that compare our performance in terms of new service connections and fault rectification for both wholesale and retail customers. We are required by law to provide equivalent service and the metrics published to date demonstrate our compliance. We believe they will continue to do so. However, because wholesale customers represent a small and non-random sample of the Telstra customer base, statistical anomalies are possible.

Another requirement relating to the accounting separation obligations is for the ACCC to publish information about the state of competition in the corporate customer segment of telecommunications markets. The first report for July – December 2003 was published in December 2004 dated June 2004. The ACCC has also published two discussion papers canvassing record keeping rules to assist the ACCC

# Competition and Regulation

to prepare the reports. We are also in discussion with the ACCC in relation to these foreshadowed rules. The requirement for accounting operation may change with the introduction of operational separation.

***Retail price restrictions***

The Commonwealth Government has set retail price controls on some of our services and groups of services that apply from 1 July 2002 to 30 June 2005, which has been extended to 31 December 2005. The Communications Minister has asked the ACCC to undertake an inquiry into the price arrangements which will apply from 1 July 2005. The ACCC has published it recommendations and the Government has announced the regime for the next 3 years. From 1 January 2006, a basket of Telstra's line rentals, local, STD, international and fixed to mobile calls will be subject to an overall price cap of CPI minus CPI. Telstra's basic line rental products will be increased only by the rate of inflation.

***CPI-X or CPI+X price restrictions***

We cannot increase the weighted average price of local calls, national long distance and international calls and fixed-to-mobile calls by more than the CPI less 4.5%. If the CPI is less than 4.5%, we are required to reduce our prices accordingly.

We have scope to increase line rental charges by up to CPI+4%. This cap recognises that basic access lines are currently priced at considerably less than the cost to provide the service and that we should be permitted to increase the line rental charge to cover costs, while at the same time reducing call prices which have, in the past, subsidised the below cost line rental. Connection services continue to be capped so that the charge for them increases by no more than the rise in the CPI.

The ACCC has powers to monitor and report on our compliance with price controls.

***Local call charges***

We and other CSPs must offer untimed local calls to:

- residential and charity customers for all local calls; and
- business customers for local voice calls.

We are not permitted to charge more than 40 cents (including GST) and after 1 January 2006 50 cents for a local call from a public payphone. This is the first price rise in ten years. We are not permitted to charge more than 22 cents (including GST) for a local call from any other service except where the higher call price is offered as part of a package that offers a lower line rental than the standard line rental. We offer reduced rates for local calls with some of our service plans.

We continue to be obliged to ensure that:

- our average price for untimed local calls provided to residential and charity customers in non-metropolitan areas in a fiscal year does not exceed the average price charged by us to residential or charity customers in metropolitan areas in the previous fiscal year; and
- our average price for untimed local calls provided to business customers in non-metropolitan areas in a fiscal year does not exceed the average price charged by us to business customers in metropolitan areas in the previous fiscal year.

***Directory assistance service charges***

We cannot impose or alter a charge for our directory assistance services without the approval of the Communications Minister. In October 1999, we commenced charging business and mobile customers for national and long distance directory assistance services after approval of the Minister. Our residential customers continue to receive these directory services without charge via the number 1223.

# Competition and Regulation

### Access

The ACCC has broad powers to determine those of our services to which competitors will have access and the terms and conditions under which we provide this access.

***Declaration of services***

The TPA creates an access regime specific to the telecommunications industry. The ACCC may declare telecommunications services or other services that facilitate the supply of a telecommunications service to be ‘declared services’. Carriers and CSPs have a qualified right to acquire declared services from other carriers and CSPs.

***Carriers and carriage service providers must comply with ‘standard access obligations’***

Unless exempted by the ACCC, carriers and CSPs who supply declared services to themselves or anyone else must comply with ‘standard access obligations’. They must provide the declared services to carriers, CSPs or content service providers who require them in order to provide telecommunications services or content services to end users.

Services not declared are not subject to regulation under this access regime. Therefore, access to non-declared services is a commercial matter, subject only to the general trade practices law.

***Current declared services***

The services which have been listed as declared by the ACCC include:

- originating and terminating access for domestic PSTN and ISDN telecommunications networks;
- terminating access for GSM and CDMA mobile telecommunications networks;
- transmission capacity on all routes (except links between mainland capital cities and some routes between capital cities and regional centres) on bandwidths of 2, 4, 6, 8, 34/45, 140/155 or higher Mbps;
- digital data access service (domestic carriage of data between exchange or other network facilities and customer premises). The ACCC has determined that DDAS and ISDN will expire as declared services in metropolitan areas after June 2006 but will continue to be declared services in regional areas;
- an unconditioned local loop service using unconditioned copper wire in our customer access network;
- local PSTN originating and terminating services (which in our view is not materially different from the domestic PSTN originating and terminating access described above);
- local carriage services (in effect, this is local call resale);
- analogue cable subscription television broadcast carriage service; and
- the spectrum sharing service (also known as “line sharing”).

***Terms and conditions of access***

A carrier or CSP may give the ACCC access undertakings which set forth the terms and conditions on which it will offer to supply declared services. An undertaking only becomes operative if it is accepted by the ACCC. The terms and conditions (including price) of standard access obligations are to be resolved by commercial negotiations. If negotiations fail but an access undertaking (including the relevant terms and conditions) has been provided by the access provider and has been accepted by the ACCC, the access undertaking will apply. If there is no such undertaking, the ACCC may arbitrate the terms and conditions on which the standard access obligation will be met.

## Competition and Regulation

***Access arbitrations***

Under the present regulatory regime, the ACCC possesses broad powers to hear access disputes relating to the supply of a declared service and to make non-appealable decisions regarding those disputes. At present, there are two access arbitrations in progress involving Telstra's supply of a declared service to an access seeker. Telstra generally attempts to avoid access arbitrations, preferring instead to resolve matters on the basis of sound commercial agreements, however this is not always possible.

***Access pricing***

The Communications Minister may make a pricing determination setting out compulsory principles for establishing access prices that must be followed by the ACCC. To date no ministerial pricing determination has been issued.

The ACCC has published general Access Pricing Principles setting out how the ACCC proposes to approach price issues when considering access undertakings and determining access disputes. In general, the ACCC proposes that the prices of declared services should be cost-based. In particular, it proposes to require access prices for such services to be based on the total service long run incremental cost (TSLRIC) of providing the service.

Telstra has been successful in having access undertakings accepted for the PSTN Originating and Terminating Services and the Local Call Service during this financial year. These being the first of such undertakings accepted by the Commission. During the same period, the ACCC rejected two other undertakings lodged by Telstra for the supply of the Unconditioned Local Loop Service (ULLS) and the Spectrum Sharing Service (SSS).

Telstra has revised its original undertakings for both ULLS and SSS, taking into consideration the ACCC's comments, and relodged the undertakings, together with new undertakings for the connection and disconnection costs for both services. The ACCC is presently assessing these undertakings and a decision is expected during the first half of fiscal 2006.

***Local call resale***

In April 2005, the ACCC commenced a full review of the regulation of local telecommunications services. The scope of the review included:

- Should local carriage service continue to be declared after June 2006 (expiry date of the current declaration)?
- How should the declared local carriage service be priced?
- Should basic access be declared?
- How should a declared basic access service be priced?
- Should the use of PSTN originating and terminating access (OTA) to provide local calls be permitted?
- Should local calls be preselectable?

The ACCC has indicated its intention to issue a final report on these issues by October 2005.

***PSTN originating/terminating access***

The ACCC has issued final pricing principles for PSTN originating and terminating services based on TSLRIC principles. Future pricing of PSTN access is also likely to be determined through the current access undertakings process and local services review.

## Competition and Regulation

### *Mobile terminating access*

On 30 June 2004, the ACCC issued a final report on mobile terminating access services. The report recommended that the existing declaration should be varied to include voice services terminating on 3G networks. At the same time, the ACCC decided not to extend the expiry date for the declaration of originating access services. The ACCC also proposed new pricing principles for mobile terminating access which are aimed at generating a gradual reduction in the price of the mobile termination access service to a level that the ACCC believes represents a closer association of price and the best cost measures the ACCC has available to it. The staged adjustment period is proposed to commence on 1 July 2004 and conclude on 1 January 2007. These pricing principles are currently subject to an appeal lodged by another carrier. Further, two undertakings with different prices have been lodged by two other carriers.

### *PSTN termination to non-dominant carriers*

The ACCC has issued final pricing principles for PSTN termination to non-dominant carriers. The ACCC determined that the charges for termination of the non-dominant PSTN networks should be based upon our de-averaged TSLRIC and that no access deficit contribution should be included in the TSLRIC of non-dominant networks. The ACCC also found that where a non-dominant PSTN network has costs significantly lower than those of our TSLRIC, the ACCC may assess whether an argument exists for looking specifically at the TSLRIC of the particular services of the non-dominant PSTN network.

### *Unconditioned local loop (ULL)*

The ACCC has issued final pricing principles for the declared ULL service based on TSLRIC principles. Future pricing of ULL services is also likely to be determined through the current access undertakings process.

### *Spectrum Sharing Services*

The ACCC announced its decision to declare the Spectrum Sharing Service (or 'line sharing') in August 2002. The ACCC's stated pricing principles for the declared Spectrum Sharing Service are based on TSLRIC principles. Future pricing of Spectrum Sharing Services is also likely to be determined through the current access undertaking process.

### *Carrier-to-carrier access obligations*

Each carrier must provide access on request to other carriers to:

- its customer cabling and customer equipment and facilities (including lines, towers, ducts and land) in place on 30 June 1991 or installed since that date using statutory powers, if it is reasonable to do so;
- information relating to the operation of its networks; and
- its underground ducts and certain of its towers and sites with the aim of ensuring that facilities are co-located on towers and in underground ducts, unless the ACA finds that co-location is not technically feasible.

Access to these facilities and information is on commercially negotiated or arbitrated terms and conditions. We have entered into a number of facilities access agreements with other carriers. The Communications Minister can determine pricing principles for access to customer cabling and equipment, network infrastructure and information relating to the operation of a network but has not done so to date.

Carriers must also comply with the Facilities Access Code issued by the ACCC in relation to access to underground facilities and certain towers and sites.

## Competition and Regulation

### Carrier licences

Carrier licences are issued by the ACA. The annual charge for a carrier licence was reduced as at 1 July 2004 from A$10,000 to less than A$1,000 plus a pro rata revenue-based contribution to industry regulatory costs.

All carriers must, as a condition of their carrier licence, comply with the Telecommunications Act, the Telecommunications (Consumer Protection and Service Standards) Act and the standard access obligations. Any breach of licence conditions is subject to a penalty of up to A$10 million.

The Communications Minister may impose conditions on any carrier licence. The Communications Minister must consult with the carrier before doing so. Our carrier licence currently includes requirements for us to:

- provide operator and directory assistance services;
- annually produce, publish and provide an alphabetical telephone directory;
- establish and maintain the IPND and provide access to the IPND to all CSPs;
- have in place and report against an approved industry development plan and comply with the plan to the extent it relates to research and development;
- extend an equivalent mobile service to those areas previously served by the analogue network (we are providing this through our CDMA network);
- develop, implement and maintain a priority assistance policy and have processes, systems and practices in place to ensure that those customers with a life threatening medical condition can be identified and provided with priority assistance;
- monitor and publicly report on the reliability of our network in designated geographical areas of Australia and, where necessary, take appropriate action to remediate a customer's service;
- provide mobile coverage in selected population centres and on selected highways; and
- make available the Internet assistance program.

### Local Presence Licence Condition

On 3 August 2005 the Communications Minister issued a new licence condition, requiring us to maintain a local presence in regional, rural and remote Australia, to the extent that this is broadly compatible with our overall commercial interests, is not unduly prescriptive and does not impose undue financial or administrative burdens on us. The licence condition requires us to prepare a plan setting out the range of activities and strategies that we deploy or will deploy to fulfill our obligation to maintain a local presence. This plan is subject to approval by the Communications Minister. Before submitting a draft plan to the Minister for approval, we are required to publish a preliminary draft of the plan and take submissions from representatives of various stakeholder groups. Once a plan is approved by the Communications Minister we are required to take all reasonable steps to ensure that the plan is complied with. Each plan can run for no more than three years.

### Carriage service provider obligations

A CSP that provides certain basic telecommunications services must provide or arrange for the provision of:

- itemised billing services;
- operator services; and
- directory assistance services to end users.

We must provide operator and directory assistance services to CSPs on request, on terms and conditions commercially negotiated or arbitrated terms and conditions. A CSP must supply information for the Integrated Public Number Database (IPND).

# Competition and Regulation

### Powers and immunities

A carrier may enter onto land and exercise any of the following powers:

- inspect the land to determine whether the land is suitable for the carrier's purposes;
- install a facility on the land; and
- maintain a facility that is situated on the land.

A carrier may only exercise the power to install a facility if:

- the carrier holds a facility installation permit, which the ACA may only issue subject to stringent conditions;
- the facility has been determined to be a 'low impact facility' by the Communications Minister (for example, specified types of underground conduit and cable); or
- the facility is a temporary defence facility.

If we engage in these activities, we must take reasonable steps to restore the relevant land and may be liable to pay compensation to land owners for financial loss or damage suffered by them as a result of our activities. We are also subject to a Telecommunications Code of Practice providing for notice and objection mechanisms. The Secretary to the Commonwealth Department of the Environment may impose conditions on some facilities installation activities.

Facilities other than those described above may only be installed with the permission of the relevant landowner and in compliance with all relevant State, Territory and local laws.

### No limitation of tort liability

The ACA has power to impose a cap on our liability in tort for damages claims but has decided not to do so.

### Number portability

Number portability allows customers to switch certain services to another CSP but keep the same telephone number.

#### *The ACA numbering plan mandates number portability for some services*

The ACA has put in place a numbering plan for Australia. Pursuant to a direction by the ACCC, the plan sets out the following rules:

- local number portability was operational on a trial basis from November 1999 and fully operational by 1 January 2000 as mandated by the ACA. There are a limited number of specific cases where an exemption has been granted;
- inbound number portability affecting all 1800, 1300 and One3 numbers became operational on 30 November 2000; and
- mobile number portability became available from 25 September 2001.

In July 2004, the ACCC directed the ACA to implement premium rate number portability. The ACA issued a discussion paper seeking comments on how to implement PRNP. Only a few submissions were received by the ACA. Because of the lack of industry interest to port premium numbers, no plan has been implemented by the ACA.

#### *Terms and conditions of supply are negotiated or arbitrated*

The terms and conditions on which CSPs supply number portability are set by commercial negotiation or arbitration.

## Competition and Regulation

The Communications Minister may make a number portability pricing principles determination that would govern any arbitration. However, no such determination has been made to date. In June 1999, the ACCC issued a paper setting out the local number portability pricing principles that it would be inclined to apply if it were required to arbitrate in relation to terms and conditions for the provision of local number portability. These principles state that each carrier or CSP should bear the costs it incurs in its own network to meet the obligation under the numbering plan to provide local number portability.

In June 2005, the ACCC finalised their decision on Digital Data Access Service (DDAS) number portability. The ACCC was not satisfied that the introduction would be likely to promote both competition and efficiency. As a result, the ACCC has not issued a direction to the ACA and disallowed Digital Network Access Service (DNAS) number portability.

***Mobile number portability***

The ACCC's final report on mobile number portability pricing principles only allows us to recover from other carriers or CSPs our efficiently incurred transit costs of providing mobile number portability from other carriers or CSPs.

**Preselection and override codes**

Preselection allows customers, while connected to a CSP, to specify another CSP to provide some tele-communications services. Override codes allow a customer to select a different CSP on a call-by-call basis.

Currently, CSPs must provide for the preselection of one CSP for the following voice calls:

- national long distance calls;
- fixed-to-mobile calls;
- international calls; and
- some operator services.

An override function for these voice calls must also be provided. The terms and conditions for provision of preselection are as agreed between the CSPs. In the absence of agreement, there is provision for arbitration by an agreed arbitrator or the ACCC.

**Interception**

Carriers are required by law to help law enforcement agencies in Australia in certain circumstances. Carriers are not expected to provide help without remuneration but they are to neither profit from, nor bear the costs of, providing such help. They must also, unless exempted by the Communications Minister or the agency co-ordinator, ensure that telecommunications services passing over their networks can be intercepted by agencies that hold an interception warrant. This requirement can lead to delay in the launch of particular carriage services until the services are capable of being intercepted.

**Universal service and digital data service obligations**

As the primary universal service provider, we have an obligation to fulfil the universal service obligation (USO) throughout the whole of Australia. This means that we must ensure that standard telephone services, payphones and any prescribed carriage service (of which none have been prescribed) are reasonably accessible to all people in Australia on an equitable basis, wherever they reside or carry on business.

As part of this obligation, we must make special customer equipment available to people with disabilities and offer interim telephone services in certain circumstances where there will be an extended delay in connecting or repairing a fault with a standard telephone service.

## Competition and Regulation

We are also a digital data service provider and have an obligation to fulfil the digital data service obligation (DDSO) throughout the whole of Australia. This requires us to ensure that all people in Australia have reasonable access to a digital data service with a data speed broadly equivalent to 64kbps. We fulfil the DDSO through the supply of ISDN services (a General Digital Data Service (GDDS)), to which at least 96% of the Australian population have access, and through the supply of BigPond® satellite 1 way services (a Special Digital Data Service (SDDS)) for the remainder of the population.

In our roles as the primary universal service provider and digital data service provider, we are required to submit plans to the ACA and the Communications Minister for their approval which set out how we will progressively fulfil the USO and DDSO throughout Australia. Our approved USO Policy Statement, USO Standard Marketing Plan and Digital Data Service Plans are available from our website at www.telstra.com.au/universalservice and www.telstra.com.au/corporate/ddsp.htm.

The Communications Minister may determine a system to select carriers to be the primary universal service providers or regional universal service provider for all or some universal services for particular years.

The net losses that result from supplying loss-making services and from facilitating the satellite subsidy for SDDSs in the course of fulfilling the USO and DDSO are required to be shared among all carriers and any CSPs determined by the Communications Minister (none have been determined). The Telecommunications (Consumer Protection and Service Standards) Act 1999 (Cwth) provides that a universal service provider's net universal service cost, as assessed by the ACA, is to be shared amongst the universal service provider and other participating carriers on a basis proportional to the eligible revenue of each carrier. The other participating carriers typically pay approximately 30% of the net USO cost determined by the Communications Minister, with Telstra absorbing the remaining cost.

For this purpose, the ACA assesses levy debits (required contributions to recognised USO costs) of other participating carriers, thereby requiring them to make payments into a universal service reserve from which payments are ultimately made to the universal service provider equal to the amount of its corresponding levy credit.

However, current legislation does not ensure that the costs we incur in providing the USO are fully recognised and properly funded by all industry participants. In accordance with the current legislation, the Telecommunications Laws Amendment (Universal Service Cap) Act 1999 (Cwth), the Communications Minister determines the net USO costs. These amounts are usually significantly less than our own assessment of the USO costs. The other participating carriers are required to pay us contributions based on the ACA assessments of their eligible annual revenue. The Communications Minister has also exercised the power to determine the cost of the USO for up to three years in advance – a previous Communications Minister has determined costs for fiscal 2005 as A$211.3 million. The net USO costs for subsequent years have recently been determined by the Minister, following advice provided by the ACA. The amounts for the next three fiscal years are $171.4 million, $157.7 million and $145.7 million.

As the primary universal service provider, we receive no contribution from other carriers for any non-recognised USO costs.

The Commonwealth Department of Communications, Information Technology and the Arts (DCITA) reviewed the USO and customer service guarantee regime and the Communications Minister tabled a report in Parliament on 17 June 2004 proposing changes to the USO funding arrangements. The recommendation for USO funding in the report is for the USO costs to be simplified and for Telstra to meet the USO legacy costs associated with legacy telephone services. However, the Government announced at the time of the release of this report that it does not intend to change the broad legislative framework governing USO costing and funding.

# Competition and Regulation

### Customer service guarantee (CSG)

At the direction of the Communications Minister, the ACA has made mandatory standards for CSPs (including Telstra) in relation to the provision and repair of standard telephone services and the keeping of customer appointments associated with these activities.

These customer service standards have been in effect since 1 January 1998 to eligible customers with five or less standard telephone services.

In accordance with the CSG Standard:

- we will connect a new standard telephone service within timeframes that range between two working days (where a telephone service has recently been working at the new premises and can be automatically re-connected) and a maximum of 20 working days (where new Telstra network infrastructure has to be provided). The actual timeframe may also be dependant upon whether the CSG customer is located in an urban, rural or remote location; and
- we will repair a CSG service in set timeframes according to the customer's location, which is either one, two or three full working days for customers located in urban, rural and remote areas respectively.

As from 1 January 2003, we reduced our connection timeframes in minor rural and remote locations where Telstra infrastructure does not exist from 6 months to 20 working days.

The damages payable under the CSG Standard include:

- for a missed appointment, A$12 for a residential or charity customer and A$20 for a business customer; and
- for a delayed connection or repair, A$12 for a residential customer and A$20 for a business customer for each working day of delay up to five working days and A$40 per working day of delay after that.

Damages cannot exceed A$25,000 per customer for each contravention.

If we have reason to believe that an event has occurred that is reasonably likely to result in us being liable to pay damages to a customer for a breach of the CSG Standard, we will notify the customer and pay those damages, whether by account credit or otherwise, within a prescribed period. This is the case irrespective of whether the customer has claimed those damages.

### Priority Assistance

The Communications Minister approved our Priority Assistance for Individuals policy on 17 June 2002. The policy aims to provide eligible residential customers, who have a diagnosed life-threatening medical condition with a high risk of rapid deterioration and whose life may be at risk without access to a fully operational phone service, with the highest level of service practicably available at the time on the connection and repair of standard telephone services. Telstra customers need to substantiate their eligibility or the eligibility of someone else residing at their premises, with certification from a medical practitioner or an authorised person.

Priority customers are entitled, unless circumstances make it unreasonable, to have a first standard telephone service connected and a fault with a nominated standard telephone service repaired within 24 hours in urban and rural areas and within 48 hours in remote areas. In addition, priority customers receive 24 hours, 7 days a week service for fault management, handling and repair. Where these timeframes cannot be met, we will offer eligible priority customers the choice between an interim priority service and an alternative service, for example call diversion to another telephone number of their choice.

# Competition and Regulation

As part of our policy, we must undertake a communications strategy to generate public awareness and advise customers of priority assistance. As at 30 June 2005, we had approximately 135,000 customers with priority assistance status.

At the request of the Communications Minister, the ACA conducted a review of our priority assistance arrangements in late 2004. In its report to the Minister, the ACA concluded that Telstra's priority assistance arrangements are largely meeting the Government's policy objectives and there appears to be a high level of customer satisfaction with Telstra's provision of the service.

**Network Reliability Framework**

The Network Reliability Framework (NRF) is an outcome of the Telecommunications Service Inquiry (Besley Inquiry) which was conducted during 2000.

The NRF was introduced through an amendment to our carrier licence conditions, which took effect from 1 January 2003, and embraces CSG telephone services only. Generally, those telephone services that are provided to customers with five or less standard telephone services.

The NRF is a compliance and reporting framework that aims to improve the reliability of our network at three different levels:

- Level 1 - 44 geographical areas throughout Australia, which are based on our work regions. We are required to provide a monthly report to the ACA on the percentage of CSG services with no faults and the average percentage of service availability for each geographical area. This information is also made publicly available on our website at www.telstra.com.au/servicereports;
- Level 2 - the exchange service area (ESA) level, of which there are approximately 5,000 throughout Australia. We are required to provide monthly reports to the ACA of those ESAs where a pre-determined number of CSG services (which is dependent upon the total number of CSG services in the ESA) have had one or more faults in each of the two preceding calendar months. The ACA can request further information from us regarding the performance of a particular ESA and may seek to have remedial action undertaken to reduce the incidence of faults in a particular ESA; and
- Level 3 - the individual service level. We are required to take reasonable action to prevent a CSG service from experiencing four or more faults in a rolling 60 day period or experiencing five or more faults in a year. Where either of these thresholds is breached, we are required to investigate the reason for the breach, undertake such remediation as is necessary and report the contravention to the ACA.

The NRF adds to the range of consumer safeguards already in place, for example the USO, CSG Standard and priority assistance.

The Australian Communications Authority conducted a review of the NRF during 2004 and provided its final report to the Minister in June 2005. The report contains a number of recommendations aimed at improving the operation of the NRF, which are being considered by the Minister.

**Supply terms and conditions**

Under a determination made by the ACA, since March 2000 CSPs that formulate a standard form of agreement relating to the supply to an ordinary customer of designated goods and services have been required to provide customers with concise summaries of the terms and conditions on which customers acquire their goods and services. We provide these summaries to existing and new customers.

# Competition and Regulation

## Hong Kong Telecommunications Regulatory Information

We own 50% of REACH which, through its wholly owned subsidiaries including REACH Networks Hong Kong Ltd (REACH Networks), conducts a wholesale connectivity business from Hong Kong. REACH Networks operates a network for the carriage of traffic to and from Hong Kong.

We also own CSL which conducts a cellular mobile business in Hong Kong. CSL holds 2G Public Radio-communication Service licences that cover the establishment, maintenance and operation of 2G cellular networks in Hong Kong. CSL also holds a 3G mobile carrier licence.

Below is a brief outline of the Hong Kong telecommunications regulatory regime and the key regulatory requirements with which REACH Networks and CSL must comply.

### *Telecommunications Ordinance (Chapter 106 of the Laws of Hong Kong)*

The legislative framework governing the provision of telecommunication services and facilities in Hong Kong is principally contained in the Telecommunications Ordinance (Chapter 106 of the Laws of Hong Kong). The Telecommunications Ordinance regulates the licensing and control of telecommunications services and telecommunications apparatus and equipment, including fixed wireline and wireless services, public mobile telephone services and certain aspects of Internet services.

The Telecommunications Authority (TA) is the principal telecommunications regulator in Hong Kong and is responsible for administering the Telecommunications Ordinance. The Office of the Telecommunications Authority (OFTA) was established in 1993 as an independent Government department and its key functions are to assist the TA in administering and enforcing the provisions of the Telecommunications Ordinance. The TA's powers include:

- issuing licences;
- making rules and determinations in relation to the provision of telecommunications network services by licensees, including setting interconnection charges on particular routes;
- requiring a licensee to comply with the terms of its licence and any applicable legislation; and
- suspending or revoking licences as enforcement measures or for the protection of the public interest.

### *Competition provisions*

The telecommunications market in Hong Kong is almost fully liberalised and is now one of the most competitive markets in the world. Unlike many countries, Hong Kong does not have a general competition law. Anti-competitive behaviour is regulated through industry specific legislation as well as in various licence conditions.

The Telecommunications (Amendment) Ordinance 2003 and its accompanying guidelines regulates merger activity in some aspects of the telecommunications industry through empowering the TA to issue binding directions to carrier licensees when certain changes in the ownership of, or the control of, a carrier licensee occur which, in the TA's opinion, have or are likely to have the effect of substantially lessening competition in a telecommunications market.

### *Second Generation (2G) licence renewal process*

The existing 2G mobile licences held by Hong Kong's mobile network operators expire in the period from July 2005 until September 2006.

Existing GSM and Personal Communication Service (PCS) licensees (of which CSL is one) have a right of first refusal. The right of first refusal entitles the GSM/PCS licensee, who agrees to the licence conditions and exercises the right, to a new mobile carrier licence which will attach special conditions and be granted in

# Competition and Regulation

respect of its existing 2G frequency spectrum. It is expected that on this basis CSL will obtain new mobile licences on expiry of its current GSM licence in January 2006 and similarly for its PCS licence in September 2006. The new licences will have a 15 year term. The Government has deferred a decision on using vacated CDMA spectrum for any new mobile licence until completion of the Spectrum Policy Review.

***Unified licensing***

The TA has indicated that 'differentiation of regulation based on fixed and mobile networks will not be sustainable' going forward, and is considering consolidation of existing mobile and fixed licensing categories and/or the creation of a new flexible licence category allowing provision of both mobile and fixed-line service. There is a risk that spectrum utilisation fees (SUF) for new services provided under this licence, eg. using broadband wireless access, will be preferential as compared to the existing SUF payable by 3G licensees. On the other hand unified licensing could have potential significant benefits for mobile operators, such as a recasting of interconnection charges between mobile and fixed-line operators and access to buildings and land on par with the rights currently enjoyed by fixed-line carriers. The unified licensing process is in its infancy and will be complex. More clarity is expected from the TA in 2006.

**New Zealand Telecommunications Regulatory Information**

TelstraClear, our wholly owned subsidiary, is the second largest full service carrier in New Zealand. Below is a brief outline of the New Zealand telecommunications regulatory regime.

***Telecommunications Act 2001***

Throughout the 1990s, the telecommunications sector in New Zealand was subject to a 'light-handed' regulatory regime. Unlike most other OECD countries, no industry-specific regulatory authority was established in New Zealand to regulate and monitor telecommunications competition and to promote efficient and sustainable entry. This light-handed approach came to an end with the introduction of the Telecommunications Act 2001.

The Telecommunications Act 2001 provides the principal framework for the regulation of telecommunications in New Zealand and grants a telecommunications sector-specific regulatory role to the New Zealand Commerce Commission (Commission). Under the Telecommunications Act 2001, the Commission's functions are to:

- make determinations on disputes between the access seeker and the access provider over access obligations of designated and specified services and also on price in the case of designated services;
- determine the net cost and apportionment (amongst industry players) of Telecommunications Service Obligations and monitor the Telecommunications Service Provider's compliance with their Telecommunications Service Obligations (broadly, a USO, for which Telecom New Zealand is the Service Provider, and a Deaf Relay Service, for which Sprint International New Zealand is the Service Provider);
- recommend to the Minister the desirability of regulating additional services where considered necessary; and
- propose and approve telecommunications access codes relating to designated and specified services for the telecommunications industry.

***Determinations by the Commission under the Telecommunications Act 2001***

The Commission has made determinations under the Telecommunications Act 2001 for TelstraClear in relation to an interim price for residential resale (made on 14 June 2004) and wholesaling (made on 12 May 2003). The Commission has also made a draft determination in relation to wholesaling for CallPlus. CallPlus subsequently settled with Telecom.

## Competition and Regulation

The Commission has made two interim price determinations for interconnection between Telecom and TelstraClear's PSTN network and for wholesale (resale) of a range of Telecom's business retail services. Telecom and TelstraClear have both sought final price determinations and these are proceeding.

The Commission has also issued a draft determination on the apportionment of costs in implementing local and mobile number portability in response to a joint application (from TelstraClear, WorldxChange, CallPlus, Compass and iHug), and on the functions and standards for number portability following a joint application from Telecom, TelstraClear and Vodafone.

The Commission made a draft determination in April 2005 on an application by TelstraClear (made in December 2004) for regulated access to Telecom's unbundled bitstream service (UBS). The Commission's preliminary view is that Telecom should provide TelstraClear with a bitstream access service available nationally with characteristics which differ from Telecom's commercial bitstream service currently available to access seekers. A final determination is expected to be made in the first quarter of fiscal 2006.

In addition, the Commission has recently recommended that the termination of 2G fixed-to-mobile calls be regulated. The New Zealand Government is currently considering whether to accept the Commission's recommendation and add the mobile termination service as a designated service under the Telecommunications Act.

***Competition Provisions***

The Commerce Act 1986 is New Zealand's generic competition legislation outlawing anti-competitive conduct in all industries and is enforceable by the Commission and by market participants.

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