The Deregulation of the Australian Telecommunications Sector: Workforce Restructuring and Employment Relations (ER) at Telstra in a Deregulated Environment

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During the 1990s successive federal governments opened the Australian telecommunications sector to competition. This paper examines how the former wholly government owned telecommunications company (TelCo), Telstra, responded to these changes, as the firm was first corporatised and then partially privatised. Telstra management introduced extensive organisational and workforce restructuring strategies that aimed to reduce costs through downsizing, outsourcing and the introduction of new technologies. Such strategies were linked to the introduction of a more unitarist approach to employment relations (ER), which included the introduction of individual Australian Workplace Agreements (AWAs). The analysis of Telstra focuses on the decade from 1990 to 2000, during which time much of the organisational restructuring and workforce reorganisation occurred. Transaction costs economics (TCE) theories are used to assist in this analysis.

Introduction

This paper begins with an examination of the background issues that led to a more competitive Australian telecommunications sector. It then considers some of the broad business strategies undertaken bv Telstra management in response the to deregulation process. These strategies associated with large organisational restructuring as Telstra evolved into a leaner firm that gained a greater proportion of its revenues from new products and services. In the process, it re-evaluated its core competencies and subcontracted work previously performed within Telstra to external firms. The paper then examines how these strategies affected employment relations (ER) practices at Telstra.

Research methods

This paper forms part of a larger longitudinal study of Telstra. The data was collected from a broad range of sources during the period 1996 to 2002. Interviews were conducted with past and present senior managers at Telstra to examine the changing nature of its workforce in the face of deregulation and privatisation.

These discussions with management were supplemented by interviews with union representatives from the Communications, Electrical and Plumbers Union (CEPU) and the Community and Public Sector Union (CPSU), who were involved with the firm. This interview data was supported by direct observations; external and internal company reports; union documents; reviews of previous research on Telstra; and other publicly available sources.

Transaction costs economics (TCE)

Researchers have used TCE theory to examine the make/buy decisions of firms (Williamson 1979; Pitelis 1996; Carroll & Teece 1999). The TCE-based hierarchy versus market model of the firm suggests certain outsourcing production processes to the marketplace may generate associated transaction costs related to opportunism and bounded rationality for example the potential loss of firmspecific knowledge to a competitor. Thus the full cost of outsourcing a service or production process to the market will include the specified market price plus any associated transaction costs. These associated costs may increase the total

price of a market transaction to the point where it is more economical to produce a good or service in-house rather than outsource the process to the market. Thus TCE can assist in analysing why Telstra maintained certain production processes and services in-house, while outsourcing other transactions. In this regard Telstra increasingly utilised human capital that was employed at arm's-length from the parent firms.

According to TCE, firms undertaking organisational and workforce restructuring would retain employees with firm-specific links strategic skills. Thus TCE processes to the downsizing assetspecificity of labour. Workers with firmspecific skills and a subsequent high degree of asset-specificity will tend to be retained, whereas the skills of more generic workers will be purchased from the market. TCE theory suggests that such strategies minimise potential transaction costs associated with make/buy decisions. all other things being equal.

Changing competitive environment

During the 1980s low productivity and a decline in international competitiveness created a perception that Australia needed to lift its economic performance. While the then federal Australian Labor Party (ALP) government did not privatise Telecom Australia — the precursor to Telstra — it recognised the growing importance of the telecommunications sector to the economy and the government's microeconomic reform agenda. In 1989 Telecom Australia became a corporation that was required to provide dividends to its owner, the federal government, raise its own investment capital and pay appropriate federal and state taxes (Evans 1988:7&22). In 1992 Telecom Australia merged with another government business enterprise (GBE), the Overseas **Telecommunications** Commission (OTC), and in the following year the new entity was renamed Telstra.

government continued its The ALP telecommunication's reform by introducing second licensed carrier. Communications, which began operations in 1992. The government then granted mobile licences to Telstra, Optus and a third competitor Vodaphone. Therefore by the early 1990s the government had created a duopoly in domestic and international services and a triopoly in mobile services (Brown 1996:3). These towards more competitive shifts a environment accelerated moves Telecom to reduce its costs to better compete with those of its competitors.

The incoming 1996 Liberal and National Party conservative coalition government was committed to further reform of the telecommunications sector and was elected with a commitment to privatise one third of Telstra. The government's objectives for the sale included the achievement of an optimum financial return and the promotion of an internationally competitive, low cost and innovative industry telecommunications (ANAO 1998:12). Critics argue as to which of these objectives was the federal government's highest priority, but the subsequent first float of Telstra shares in 1997 was highly successful.

The success of the initial Telstra share sale added momentum to the government's privatisation policy, so that the government went to the 1998 federal election with a commitment to sell a further 16.6 per cent of Telstra. allowed the government to retain majority ownership, with 50.1 per cent of Telstra shares remaining under government It was envisaged that full control. privatisation of the company would follow after an independent enquiry was satisfied that concerns over Telstra's universal service obligations to regional areas were adequately addressed. But although it was returned to power in the lower house, the House of Representatives, the government failed to gain a majority in the upper

house, the Senate. In mid-1999 the Senate agreed to the sale of a further 16.6 per cent of Telstra, but remained opposed to any sale of the remaining 50.1 per cent of the firm.

Deregulation

The Telstra and Optus duopoly and the mobile telephone triopoly were phased out on 1 July 1997 and replaced by an open deregulated market. However, Telstra retained its ownership of the public network. Deregulation fostered more competition and by the late 1990s there were 21 licensed carriers operating in the Australian market (Telstra 1998:4).

This increase in competition was against the background of a rapid increase in the size of the Australian telecommunications market. During the 1990s the Australian telecommunications market grew at close to 10 per cent per annum, with data transmission increasing at an even more rapid rate (Switkowski 2000). Thus the market was approximately doubling in size every seven years. Such rapid market growth allowed Telstra to increase sales and revenue in the face of new competitors and declining market share.

Following a decade of strong growth, the period from 2001 to 2002 witnessed a slowing down in the growth rates of the telecommunications sector. The collapse of the dot.com and TelCo stock market bubble of the late 1990s also caused a shake up in the telecommunications market. In 2001 the Singaporean owned TelCo, SingTel, purchased Optus as a 100 per cent wholly owned subsidiary (Ellis 2001:34-36), while other smaller local competitors, such as OneTel, went into liquidation. Telstra's share price dropped to some of the lowest levels seen since they were first floated in the late 1990s. but it continued to be a very profitable enterprise.

Business strategies

Telstra management responded to competition by shifting the firm towards a

more commercial orientation that included organisational restructuring and labour cost reduction strategies. The latter were achieved through outsourcing, downsizing and the introduction of new technologies. Between 1989 and 2001 Telstra reduced its full-time workforce from approximately 84,000 to less than 45,000 full-time workers (Telstra annual reports). strategies fuelled political and community Telstra's concerns that commercial focus would cause it to reduce services to less profitable rural and regional areas.

During the 1990s senior management redefined their notions of what constituted Telstra's core competencies and functions. In 1990, Telstra saw itself as a telephone company whose primary aim was to connect a telephone to every person in Australia (Interview with Telstra 2002). But while the carriage of basic telephony remained a large revenue source for Telstra, it was seen as being increasingly lower value-added service subject to downward pressures on prices. Telstra's \$2.1 billion half yearly profit report for 2000 showed that for the first time, its combined revenues from newer technologies — such as mobile phones, email, data and internet related services outperformed its traditional revenue base of local and long distance calls (Gilchrist & Elliot 2000; O'Brien 2000).

Outsourcing and downsizing

1990s Telstra During the created subsidiaries and entered into joint ventures that provided services previously conducted within the core firm. It also engaged in partnerships with other firms that complemented its existing skills and infrastructure. These latter firms often provided content and services that could run over Telstra's network. In the process Telstra focused on new products and services that were contributing increasing proportion of its revenues. Conversely older, more traditional TelCo services — such as the work performed by

operators — were outsourced to the marketplace. These strategies decreased the size of Telstra's core firm.

maintained that Senior managers redundancies that resulted from outsourcing were not forced, with many employees having the option of joining these new enterprises. Telstra's CEO, Ziggy Switkowski, advised that this process "allows employees to think more expansively about their (Switkowski 2000), the implication being that Telstra workers should consider job options outside of the core firm. However, conditions of employment in these new subsidiaries and alliances did not mirror those at Telstra, as joint ventures firms introduced more "flexible" enterprise agreements.

Telstra argued that such reductions in staff numbers were necessary to make the company more attractive to potential shareholders and to achieve world best practice. Telstra used the services of Mercer Consultancy to benchmark it against a group of North American TelCos. The results of this study suggested that the company was performing at around 30 per cent below American standards. Management then concluded that this equated to a need to reduce staff numbers by around the same level — 30 per cent (Telstra 1995:12; SERCARC 1996). But international benchmarking comparisons such as these are difficult, given the differing geographical, political legislative constraints within which TelCos operate. The unions disputed the criteria used to achieve the report's benchmarking results and conclusions and highlighted the differences in the operating environments between Telstra and the firms studied (SERCARC 1996).

Despite union objections this benchmarking study was subsequently used to support the internal management restructuring program, "Project Mercury", that examined ways to reduce workforce numbers. The program targeted "non-

core" functions for redundancies and outsourcing. The objective was "to ensure that staff without necessary skills and experience are exited from the company in an effective and timely manner" (SERCARC 1996).

In the late 1990s Telstra accelerated this downsizing program, as management sought to reduce costs in the now partially privatised firm. Between 1997 and 2001 Telstra reduced its full-time workforce by almost one third. Telstra's 2001 annual report stated that it had a permanent of approximately workforce employees. But this figure included workers employed by Telstra subsidiaries. such as NDC and Pacific Access. If these employees were excluded from the figures, then by 2001 Telstra employed less than 40,000 workers — a large decrease from the 84,000 workers that it employed in 1989.

Workforce restructuring

Thus changes to Telstra's workforce reflected management's redefinition of competencies and Telstra's core organisational restructuring and outsourcing strategies. Telstra began by outsourcing generic work. This included targeting tradespersons in areas not specifically associated with telecommunications. Because Telstra had traditionally performed most of functions in-house it had employed and trained tradespersons in many diverse areas. These included motor mechanics. tool makers and wood machinists (Telecom 1990:188). By 2001 many of these job classifications had disappeared.

Other generic work outsourced by Telstra building services, drafting, included caretaking. cleaning. food services. materials distribution and property management (Interview with Telstra). Targeting generic work for outsourcing accords with a TCE approach downsizing (see Williamson 1979). This work has a low degree of asset specificity,

which reduces the potential loss of firmspecific skills and/or core knowledge from the firm.

In the mid to late 1990s Telstra targeted semi-skilled work, such as operator services, for outsourcing. Telstra operators had received wages and conditions that were higher than the market average, which provided an added incentive for management to outsource this work. Therefore in 1998 Telstra began to outsource its call centre work to the joint venture firm Stellar. This included directory assistance, sales and billing enquiries jobs. Telstra also made greater use of casual and fixed term operator staff (Eason 1998:9).

Telstra managers and union officials advised that many experienced operators chose not to shift across to the new employer, Stellar. The reasons were related to perceptions of less favourable working conditions under the new employer and because many workers chose not to move to where the new centralised call centres were being set up (Interviews with Telstra & CEPU).

The loss of experienced Telstra staff led to initial problems with quality control in the new entity and to associated customer complaints (Interview with Telstra 2002). Operators are often the first contact points for customers dealing with Telstra, so a bad experience can alter a customer's perception of the firm; an associated potential transaction cost. Thus a TCE approach to outsourcing this process would need to balance immediate cost reductions against potential quality control issues associated with outsourcing operator The Stellar workforce also work. exhibited higher worker-turnover rates than did Telstra operators. This lack of experience amongst Stellar operators relative to Telstra operators would suggest a lower quality of service. But Telstra managers maintained that many of these problems were resolved over time. Telstra's decision to continue shifting its operator services work to its joint venture partner Stellar suggests that labour cost reductions were an overriding factor in this decision.

New technology allowed Telstra to centralise and reduce the number of its call centres. Telstra managers advised that this rationalisation process was extremely time-consuming, as the closure of call centres attracted considerable political and community pressure; a further transaction cost.

During the 1990s Telstra also reduced the size of its semi-skilled communications officer field workforce: in terms of total worker numbers, these were some of the largest job cuts to occur. These workers performed linesman and basic telephone installation work, along with some generic pit and pipe work. Much of this work was then outsourced and/or superseded by new technologies. Telstra also introduced new work practices for the remaining employees that increased productivity, but regarded unions this intensification (Interviews with Telstra & CEPU).

Telstra also moved beyond the above strategies of outsourcing generic and semiskilled work, as it began to outsource higher skilled jobs. This included its higher skilled technical work. As with the communication officer classification, Telstra engaged in redundancies to reduce labour costs within what was a relatively large section. Therefore by the late 1990s Telstra was outsourcing an increasing amount of its technical work to external contractors. This strategy was reinforced by Telstra's decision in 1999 to shift its network construction and maintenance work to the new subsidiary (discussed in greater detail below).

Moves to outsource higher skilled work were also reflected in Telstra's 1997 agreement to outsource its IT support work to the newly created joint venture, IBMGSA. The decision to outsource IT

support work was related to cost and the belief that Telstra's joint venture partner, IBM, could do the job better. managers argued that IBM could provide the technical upgrades that were required in the fast changing IT world in a more cost efficient manner. Telstra's previous IT infrastructure had been mainly built by Telstra IT workers and was in many respects unique to the firm. While this gave Telstra workers a large degree of firm-specific expertise in Telstra's IT network, it implied that new IT upgrades should be built within the firm. Where Telstra did attempt to buy IT systems "off shelf" thev generally required extensive modifications before they would work on Telstra's system. Given the size of Telstra's IT operations this created high costs whenever the firm was changing and/or upgrading its IT processes, such as its billing systems (Interview with Telstra 2002). Therefore, Telstra hoped that IBM Telstra's shift IT requirements into a more generic format, while IBM's extensive IT products and skills base would allow the joint venture to more effectively keep up with the market at a substantially reduced cost (Interviews with Telstra 2002).

The IBMGSA joint venture led to the loss of a great deal of in-house IT capability, but it allowed Telstra to operate a more generic IT system. In this environment the firm-specific skills of the former Telstra IT workers became less valuable to the firm. IT workers at IBMGSA required less firmspecific training and could be more easily brought into the joint venture from the external market. Therefore this shift from a firm-specific to a more generic IT system made it easier for Telstra to outsource IT jobs. However, Telstra retained some of its highest skilled IT workers for more firm-specific R&D and problem solving purposes within the core firm (Interview with Telstra 2002).

Strategic partnerships

Telstra decided to create content for its internet networks via its joint ventures and/or strategic partnerships with other firms (Switkowski 2000). While these partnerships did not impinge on current Telstra jobs, new jobs in content creation were being created within these external firms. Telstra's business strategies identify these markets as potential growth areas, which limits the growth of the workforce in the core firm. Thus the workers involved in developing these markets will many instances not be employees but, instead, will increasingly come from subsidiaries and/or alliances. Therefore, Telstra's income from these newly emerging markets will continue to rise; however, this will not necessarily lead to any corresponding increase in the number of workers employed by Telstra. Rather, evidence suggests that the core workforce at Telstra will continue to decline, at least in the short to medium

Network Design and Construction (NDC)

The NDC section was responsible for building and maintaining Telstra's public network. However, during the 1990s Telstra introduced greater contestability into these operations by offering tenders to external contractors (Barton & Teicher 1999:14-15). This initial outsourcing of technical work was generally confined to smaller jobs and/or support roles for Telstra's workforce, but more skilled technical work was outsourced over time.

Following a reduction in Telstra's capital expenditure in the late 1990s, senior management decided that the NDC section no longer constituted core business. Interviews suggested that this was not a universal sentiment and that middle managers in particular were concerned about the loss of these skilled workers (Interviews with Telstra & NDC 2002). Nevertheless, in 1999 NDC was shifted out of the core firm and made a subsidiary of

Telstra. It therefore became an employer in its own right. Telstra then put the subsidiary up for sale (Elliot 1999).

Union unions officials saw the sale of NDC as a short term cost cutting strategy (Interviews with CEPU 2000-2002). They suggested that moving NDC out from the core firm provided Telstra with a relatively quick way to reduce costs, while the eventual sale of the subsidiary would produce a further financial windfall (Interviews with CEPU 2000-2002).

This strategy meant that Telstra became more reliant on the external market to provide the required technical expertise to maintain and upgrade its infrastructure. Therefore in the late 1990s Telstra began to foster an external telecommunications engineering industry. The creation of such a contestable market would allow Telstra to place future large-scale capital investments out for tender. To assist in this process Telstra created a "Contract Management Unit" to oversee its tendering arrangements, which included contestable and non-contestable work. In 2002 the non-contestable work was still reserved for NDC. However NDC was required to bid against competing firms in the external market for any contestable work. In the late 1990s NDC competed against at least 18 other firms (Elliot 1999).

In 2002 Telstra reduced the amount of non-contestable work it allocated to NDC by approximately 30 per cent (Interview with NDC 2002). NDC managers advised that Telstra then planned to eventually make all its work contestable in the This reduction in external market. guaranteed non-contestable Telstra work reduced NDC's market value. concurrent slump in Australian the telecommunications sector also compounded NDC's problems as there was little demand from other TelCos for contractors, such as NDC, to build and maintain new telecommunications networks. This led NDC to substantially downsize its workforce. While Telstra had been keen to sell its subsidiary, in 2002 it was still unable to find a buyer willing to pay its \$1 billion asking price. Therefore in early 2003 Telstra re-absorbed NDC back into its core firm.

Despite its failure to sell NDC, Telstra continued to foster a more contestable external market for its technical work. In 2002 it set up the Total Area Service Management (TASM) **Project** benchmark Telstra technicians against outside contractors. The object was to assign contractors their own projects and areas that could then be compared with the work performed in projects and areas assigned to Telstra technicians. The use of subcontractors and the implied threat of perhaps losing their jobs induced Telstra technicians to reduce their costs. Thus the introduction of competition enabled Telstra gain cost reductions from both subcontractors and its own technicians.

The use of subcontractors also gave Telstra greater numerical flexibility to manage changing workloads, as subcontractors could be called in to supplement Telstra's existing workforce during peak periods (Interview with Telstra 2002). But Telstra managers found some limitations with these strategies. For example, when they studied the Telecom New Zealand model where most technical work was outsourced — they found that every time it rained and the network was damaged it cost Telecom New Zealand large amounts of money to get subcontractors to perform this work These subcontractors had little incentive to reduce fault rates, as the more faults they repaired the more money they received. Telstra managers suggested that Telecom New Zealand was now paying bonuses to subcontractors who could reduce their fault rates (Interview with Telstra 2002).

Union officials also claimed that the work performed by subcontractors was of a lower quality than that performed by Telstra technicians. They further alleged that Telstra technicians were frequently required to fix mistakes that were made by subcontractors (Interview with CEPU 2002). Thus perceived limitations in the use of subcontractors caused Telstra to retain some in-house technical capability.

Employment Relations (ER)

The above organisational and workforce restructuring strategies impacted on Telstra's ER polices, as management sought to introduce more flexible employment practices. This included breaking down demarcation lines and increasing the span of working hours.

Australian federal ER legislation during the early to mid-1990s allowed a greater role for awards in setting employment conditions and restricted the introduction of individual contracts for workers. Unions had long been a strong force within Telstra and under the former federal ER thev were able system to considerable influence. The links between the former ALP federal government and the union movement also made large-scale redundancies and outsourcing decisions more difficult. These external factors helped to steer Telstra management towards a more conciliatory ER process in the early 1990s known as the participative approach.

Interviews among the various stakeholders at the firm level elicit different responses as to the effectiveness of the participative approach (Interviews with Telstra & CEPU). The unions had tended to see the participative approach as an agreement between unions and management that could develop into something similar to co-determination. However, management viewed the participative approach more as a strategy to incorporate employees and their unions into the implementation of organisational change and thus pre-empt their opposition to it. Thus management saw the approach as a communication process with unions and workers rather than as a form of co-determination (Interviews with Telstra & CEPU).

The incoming 1996 conservative coalition government, with its industrial relations reform agenda and its commitment to partially privatise Telstra, heralded a change in management's ER strategies. Telstra then shifted towards more unitarist style ER practices. The participative approach was abandoned and management developed a much tougher attitude towards the unions. The provisions of the Workplace Relations Act (WRA) 1996 assisted management in these strategies. The former single collective agreement was split into a number of smaller enterprise agreements, which fragmented the workforce. Meanwhile the majority of middle managers were moved on to Australian Workplace individual agreements (AWAs) contracts.

Telstra also aimed to shift employment conditions out of awards and EBAs and into company policy manuals. A potential problem with this approach is that policy, as opposed to an award or EBA provision, can be changed unilaterally by management without the workers' and/or unions' consent.

During the 1990s Telstra also changed its approach to training. Many Telstra technicians had high skill levels that were built up over a long career within the firm. However, Telstra management no longer attached such a high importance to long term worker commitment and increasingly viewed staff turnover as part of the rapidly changing telecommunications sector. This reduction in technical training led to concerns over possible future skills shortages that have the potential to drive up future labour costs (Interviews with Telstra & CEPU).

Despite these changes, Telstra management did not succeed in all their ER strategies. While the AIRC removed a number of former Telstra award provisions under the WRA's award simplification process, it also retained some award provisions that Telstra had sought to remove. Secondly, despite Telstra's

success in moving its managers on to AWAs, the majority of its workers remained covered by collective agreements rather than individual contracts. Union membership amongst these latter workers remained relatively high, while Telstra also agreed to substantial wage rises throughout the 1990s.

Conclusion

Telstra's transition from a GBE to a partially privatised corporation saw its organisational structure change, as it adjusted and redefined its strategies in the face of changing technologies and increased competition in a deregulated market. By the end of the 1990s Telstra operated a smaller core firm supported by subsidiaries, joint ventures and strategic partnerships.

Within this changing environment Telstra operated under a number of external constraints. These included majority federal government ownership politically sensitive universal service obligations that required Telstra to provide comparable telecommunications services across a sparsely populated continent. government continued federal majority ownership pressured Telstra to pursue social and politically sensitive objectives that could impinge on its future profits.

Telstra's organisational restructuring was associated with downsizing strategies. Telstra managers advised that outsourcing was a significant factor in the downsizing process, as Telstra outsourced work that was no longer considered "core business". However, new technologies and "better" practices — including intensification — also played key roles in cutting the size of Telstra's permanent workforce (Interview with Telstra 2002). Telstra initially targeted generic and semiskilled work, but in the late 1990s it began to outsource higher skilled work, such as that performed by IT workers and technicians.

Telstra attempted to foster a competitive market for its future network building and maintenance work; however, by 2002 the external market could not provide all the technical field services and expertise that Telstra required. Thus Telstra retained an in-house technical capacity to cover areas where the use of contractors had proved less than optimal. Telstra's failure to sell NDC increased this in-house technical capacity, as some of these workers were re-absorbed back into Telstra's core firm.

Telstra also targeted higher skilled IT jobs for outsourcing. Telstra managers considered the idiosyncratic nature of its IT network and the subsequent firmspecific skills of its IT workers as a competitive disadvantage. In this instance a more generic IT system and associated IT skills were considered to be a cheaper and more effective alternative.

TCE provides some support for the organisational restructuring and outsourcing strategies undertaken by Telstra subsequent to corporatisation. In particular it supports the outsourcing of generic work. TCE also largely supports the outsourcing of semi-skilled work, such as operator services, though with some qualifications with regard to issues, such as quality control. TCE has more difficulty in supporting the outsourcing of skilled technical work associated with the building and maintenance of Telstra's network. These workers gained a high degree of firm-specific skills — and high asset specificity — and a TCE analysis would suggest that these workers should be kept within the core company. This leaves Telstra open to criticism that outsourcing this firm-specific technical work was simply a strategy to reduce short term costs after it had completed its latest capital investment program.

Williamson states that to economise, a firm must minimise the sum of production and associated transaction costs, such as bounded rationality (1979: 245). Thus a firm that outsources a service and/or

production process generally loses some control over that process. Telstra retained the ability to influence the strategies of many of its joint ventures by maintaining a controlling interest and/or substantial equity in these entities. This degree of influence reduced bounded rationality problems associated with outsourcing. Telstra shifted many of its own workers to these new entities, which allowed it to continue to make use of their skills.

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In 2003 Telstra was the dominant carrier in the Australian telecommunications sector and remained very profitable. However conservative federal the government remained committed to the privatisation of the firm. Such an option is likely to lead to more large-scale organisational and workforce restructuring at Telstra, along with further shifts towards a more unitarist approach to ER.

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