Competition Regulation of Telecommunications

Brian Johns discusses the regulation of competition in the telecommunications industry

The pace of microeconomic reform in Australia's telecommunications industry is accelerating. Yet it will be several more years before we can pass judgment on the effectiveness of the arrangements now being put in place for the regulation of the industry and the promotion of competition. To be successful the new arrangements should:

- provide an incentive for adequate investment in telecommunications;
- ensure that prices to consumers decline in accordance with the cost savings resulting from this investment and the related improvements in technology; and
- lead to effective long-run competition in basic carriage services.

Telecommunications Act

The *Telecommunications Act* 1991 specifically authorises certain acts in the telecommunications industry, thus conferring on them immunity from the operation of the *Trade Practices Act*. Section 236 of the *Telecommunications Act* specifically authorises acts that are necessary to comply with, or give effect to:

- a condition of a carrier's licence or public mobile licence;
- a direction or determination by the Minister or AUSTEL under the Act (including an International Code or Practice to be determined by the Minister); and
- a registered access and interconnection agreement.

The telecommunications industry is also in a special situation, at least prior to 1997, because of:

- the merging of Telecom and OTC which confers on the merged entity, the Australian and Overseas Telecommunications Commission (AOTC) a degree and market power greater than they individually possessed;
- the statutory duopoly in basic carriage services which precludes entry by additional competitors;
- the regime for regulating competition which, unlike general competition enforcement policy, provides for Licensing schemes, Ministerial Determinations and AUSTEL direction powers in relation to certain specified Carrier activities; and
- the powers that Austel has to ensure fair competition between the carriers and between the carriers and service providers.

While this degree of regulation of competition is unusual, it is said to be justified be the need to ensure a smooth transition from a regulated monopoly to an environment of eventual open network competition. The competitive safeguards are viewed by the Government as being of paramount importance in:

- assisting, in the short term, the second carrier in overcoming the formidable marketing advantages AOTC possesses; and
- introducing, in the long term, genuine and sustainable network competition.

The aim is to ensure that by 1997 there is a significant network competitor to AOTC. The *Telecommunications Act* does not attempt to prescribe the post-1997 environment. Indeed, after 1997, it is likely that the *Trade Practices Act* will apply to telecommunications as it does to other markets.

Viable competitors

The provisions of the *Trade Practices Act* are not designed to confer a temporary competitive advantage on new entrants to an industry so that they will remain viable in the long-term. However, the Act does offer some protection to entrants against the misuse of market power by a large rival which is already established in the market (section 46).

Some of the provisions of the *Telecommunications Act 1991* tilt the playing field slightly more in favour of the new competitor in basic carriage services than would be usual if the *Trade Practices Act* applied alone. The primary mechanism for assisting the new carrier is the interconnection rights under the *Telecommunications Act*. There are other mechanisms. For example:

- AUSTEL can direct the dominant carrier to unbundle its basic carriage services and supply a particular service;
- a dominant carrier will be required to charge strictly in accordance with its tariff;
- a dominant carrier will not be able to discriminate between customers.

For practical purposes, the dominant carrier is AOTC. The logic of these requirements on AOTC is straight-forward — the dominant carrier has the market power to restrict entry and there is the need to ensure the prospective new carrier is given a fair chance to compete.

The role of Austel

There is a relatively clear demarcation between those markets in telecommunications in which AUSTEL has a responsibility to foster and promote competition and those where the Trade Practices Commission has sole responsibility, through the provisions of the *Trade Practices Act*.

The central feature of the *Telecommunications Act* is the framework it provides for the introduction of sustainable network competition. A crucial element in introducing such competition is the new carrier's ability to interconnect on an equal basis to AOTC's network and ancillary facilities.

In these areas, AUSTEL is given a clear mandate to create the conditions necessary for genuine competition between the two carriers. It has the power to:

- register interconnection agreements;
- arbitrate on disputes over access terms and conditions; and
- make determinations on the terms and conditions that will apply.

The *Telecommunications Act* also provides the framework for fostering competition between carriers and service providers. In this area, AUSTEL again has the prime responsibility for maintaining competition. It has the power, for example, to:

- direct a dominant carrier to unbundle a basic carriage service, particularly if the failure to unbundle would lead to a substantial lessening of competition within the meaning of the *Trade Practices Act*.
- direct a carrier to comply with an accounting separation regime. This may be needed to identify and prevent cross-subsidisation by a carrier, particularly if parts of a carrier's business not facing strong competition are being used to subsidise predatory pricing.

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The *Telecommunications Act* contains a number of other competitive safeguards against particular abuses of market power by carriers, including a prohibition against a dominant carrier discriminating between its customers. However, in this matter it is up to aggrieved parties to apply to the Federal Court for relief under the *Telecommunications Act*.

The role of the Commission

The Trade Practices Commission's role in the promotion of competition is mainly in regard to the higher level services and in the equipment markets for telecommunications hardware.

There seems no doubt that the Trade Practices Commission can proceed to take action against:

- third-line forcing (where a supplier, for example, insists on bundling together equipment and services) (section 47);
- other exclusive dealing arrangements (section 47);
- predatory pricing (where it constitutes a form of misuse of market power within the terms of section 46);
- anticompetitive agreements (other than carrier interconnection and access agreements) (sections 45 and 45A).

Nevertheless, some limitations on the powers of the Trade Practices Commission need to be noted. These arise from the wording of the *Trade Practices Act*:

- The provisions of the Trade Practices Act dealing with resale price maintenance (section 48) and price discrimination (section 49) apply to goods only — services are not included. The Commission has suggested publicly that services be included in the relevant sections of the Act, but at the moment the anomaly remains.
- The merger provisions of the *Trade Practices Act* (section 50) require dominance in a market before the Commission can act against the merger. However, dominance is a high threshold which can let through some mergers which nonetheless may have substantial anticompetitive effects. For example, the Commission is of the view that the merger of OTC and Telecom's business interests in value added services may have anticompetitive effects, but it does not result in the necessary market dominance such that the *Trade Practices Act* would be invoked. The Commission has publicly suggested that the effectiveness of the merger provisions would be enhanced if the dominance test were changed to a test of substantially lessening competition.

Between the clearly demarcated areas of responsibility of AUSTEL and the Trade Practices Commission, there is a grey area where the roles of the two organisations could overlap. The Government has recognised a potential for conflict in this area by including in the *Telecommunications Act* statutory provision for AUSTEL to refer complaints to the Trade Practices Commission where it forms the opinion that the matter could be more effectively dealt with by the Commission.

Carrier connection obligations

The issue of access and interconnection has been mentioned earlier. Government policy requires AOTC to provide interconnection on a directly attributable incremental cost and equal access basis. The former Transport and Communications Minister, Kim Beazley, announced that the interconnection charges will only apply until the second carrier gains sufficient market power to negotiate effectively with AOTC on an equal basis.

However, there is a broader question of whether it should be obligatory for a carrier to supply all who require access to the service on reasonable terms and conditions.

The United States Courts have held that a firm which controls a facility essential for competition, and which cannot be readily duplicated, cannot exploit its control over that facility by unreasonably refusing to allow competitors access to it.

Competitive concerns arise because of the likely effects of such monopolisation on markets in the form of higher prices, excess profits and because of the possible use of monopoly positions to leverage monopoly power into upstream or downstream markets. To completely allay competitive concerns, access would have to be open to all genuine users, and the price and conditions of access to such users reasonable.

Natural monopolies

However, even aside from the difficulty of determining the criteria for genuine use, natural monopoly arises because it is the cheapest way of providing a service. This raises the principle that the application of competition law should ideally not impose access requirements which adversely impact on the efficiency of a natural monopoly. In some cases open access could dampen incentives to expand or construct new facilities.

In Australia these issues are emerging, particularly with deregulation. The application of section 46 to require the owners of essential facilities to provide access to them on reasonable terms is a contentious issue. However, the Commission believes that where the owner of an essential facility is vertically integrated, is unregulated and is using its power in the market to eliminate or reduce competition, a contravention of section 46 is likely to occur.

Relevant considerations for the Commission in deciding access matters would include the following:

- if the facility can be seen to have substitutes, or there are other viable options for the entity denied access, then it is doubtful a misuse of market power exists;
- whether there is a legitimate commercial reason for denying access, such as capacity or cost factors;
- whether there is a history of access to the facility in the past;
- whether the corporation controlling the facility is also competing in downstream or upstream markets and if so whether denial would have the effect of lessening competition in these other markets; and
- whether enforced access to the facility would act to take away from firms the fruits of commercial risk-taking.

The Commission has some concerns about the effectiveness of section 46 in all those cases where the Commission considers action should be taken. A general concern is that it was not drafted specifically to deal with issues involving natural monopolies. A second concern is the high burden of proof under section 46 where anticompetitive purpose must be shown. The Commission has previously raised for public consideration the replacement of the current purpose test in section 46 with an effects test.

Conclusion

The Government has opted for industry-specific regulation to overcome the problem of access in the telecommunications industry. However, in the post 1997 environment, a more generally applicable approach may be more effective, given that many of the issues transcend just one industry.

In the period up to 1997 there will only be one competitor to AOTC in the provision of basic carriage services. The role of AUSTEL — in conjunction with the Trade Practices Commission — in promoting early and effective competition will be pivotal.

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