Fair Trade Commission Disposal Directions (Policy Statements) on the Telecommunications Industry

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1. Background

Traditionally, telecommunications enterprises have been regarded as being natural monopolies. However, with the advancements in wireless and digital communications technologies, the natural monopoly theory of telecommunications industry has gradually been challenged. The network interconnection between several telecommunications enterprises may lead to positive production and consumption externality while, in response to the developments of digital convergence, consumers' demand for telecommunications services has also shifted from conventional voice services to integrated digital, visual, and multimedia services. Despite the fact that telecommunications enterprises are subject to regulatory oversight by the competent authority in charge of telecommunications industry and most of activities of the telecommunications enterprises shall be governed by the telecommunications-related regulations, conducts such as businesses engaged in various forms of restrictive or unfair competition could constitute violations of the Fair Trade Law (hereinafter referred to as "the Law"). The Fair Trade Commission (hereinafter referred to as "the

Commission") has therefore gathered and analyzed pattern of practices in the telecommunication industry that may violate the Fair Trade Law and accordingly adopted the Policy Statements under the framework of the existing statutes and regulations. The adoption of the Policy Statements aims at helping related enterprises avoid violations of the Law and at the same time serving as a reference for handling future cases by the Commission.

2. Terminology

The terminologies referred in the Policy Statements are as follows,

A. Essential Facilities: The terminology refers to the following facilities:

(1) the facilities are owned or controlled by a monopolistic enterprise;

(2) competitors are financially and technically unable to replicate or replace the facility at issue within a short time';

(3) competitors are unable to compete with the owner or controller of the facility in the relevant market if they are denied use of the said facility;

(4) the enterprise that owns or controls the facility at issue has the ability to provide such facility to its competitor.

B. Ramsey pricing: Ramsey pricing means when the total income equals the total costs, the supplier charges consumers with lower demand flexibility higher prices and consumers with higher demand flexibility lower prices in order to gain maximum social surplus without affecting its normal operation.

3. Market Definition

The relevant market for telecommunications industry is defined in accordance with the Commission's "Guideline on the Definition of Relevant Market". In addition, the business model, transaction characteristics, business nature, technological development and other factors of telecommunication enterprises will also be taken into account when specific cases are concerned.

Example 1. Do ADSL and cable modem services belong to the same product market?

Presently, cable broadband (including ADSL, cable modem and leased line) and wireless broadband services that telecommunications or cable TV operators provide are the major methods of Internet access for most home-users. Both ADSL and cable modems allow high-speed access with the always-on function. The rate terms and calculation criteria are also similar. Therefore, ADSL and cable modem services can be regarded as belonging to the same product market.

Example 2. Do telecommunications operators belong to the same market when they provide reception services?

Under the caller-pays system, when a subscriber calls users outside the network, the provider has to purchase "termination service" from the telecommunications service provider of the call receiver in order to put the call through. Therefore, do telecommunications operators belong to the same market when providing reception service? Oftel and the Competition Committee of the UK, when reviewing cases concerning the charges for call receivers, concluded that (1) the call terminating network is susceptible to traffic jams since all calls made to people subscribing to the same telecommunications service provider had to be processed through the network designated by the said provider and there was no other substitute route; (2) the call terminating network was chosen because of the call receiver yet caller had to pay for the reception charge and this is "call termination externality;" (3) the caller was not a subscriber to the call terminating network and, therefore, customer loss would not be a concern even if the reception charges were high; (4) call receivers usually were careless about the reception charges their provides determined. Under such circumstances, if there are no proper rate regulation and reciprocity agreement between interconnected telecommunications service providers, the call originating networks are not powerful enough to rival, and all providers of termination service make "small but significant non-transitory increases in price." Despite that all the telecommunications operators belong to the same retail service market, it is possible that each operator is deemed as operating in an independent market in cases where provision of termination service is concerned.

4. Market Share

The market share of a telecommunications enterprise may be calculated in accordance with the following methods:

A. the percentage the number of subscribers to a specific telecommunications enterprise in the total number of subscribers to all telecommunications enterprises in the relevant market: the market share of each telecommunications enterprise is calculated according to the numbers of subscribers to telecommunications enterprises the Commission has obtained through the investigations it conducted or the statistics the competent authority provided on a regular basis.

B. the percentage of the amount of sales or revenue of a specific telecommunications enterprise in those of all the telecommunications enterprises in the relevant market: If the numbers of users of some telecommunications services are uncertain (such as those of long distance, international and pay phone calls), the calculation can be conducted based on the percentage of the amount of sales (such as the aggregates of long distance and international call minutes, the number of messages or packages sent, the number of pay phones) or the total revenue in the total amount of sales or revenues in the relevant market.

C. the productivity a specific telecommunications: When there's no data on the number of subscribers, sales and revenue, the capacity of a specific telecommunications enterprise to provide products or services (such as the number of circuits owned, the quantity of bandwidths, telecommunications numbers or IP addresses approved) can also become one of the elements considered in market share calculation.

5. Monopoly

The following practices of telecommunication enterprises with the monopolistic market power may become violations of Article 9 of the Fair Trade Law:

A. predatory pricing: This refers to situation in which an enterprise sacrifices its short-term profits and set prices far lower than its costs to force its competitors to withdraw from the market or obstruct potential competitors from entering the market in order to obtain excessive profits in the long run unless the circumstances of setting price at a below-cost level are for short-term period promotions originating from legitimate business act, or are due to the unexpected increase in costs or other legitimate reasons.

B. vertical price squeeze: A vertical price squeeze occurs when a vertically integrated telecommunication enterprise dominant in an upstream market supplies an essential input to its competitors in a downstream market on which the dominant enterprise is also active. In order to impede or exclude its downstream competitor, the vertically integrated enterprise could then raise the price of the upstream product (service) and reduce the price of the downstream product (service) or behave in other similar manners so that an efficient downstream competitor is forced to exit the market.

C. improper cross-subsidy: This refers to a telecommunication enterprise providing a number of services uses revenues from its exclusive service to subsidize losses occurring on its competitive service, or uses revenues from the regulated service to subsidies losses occurring on the unregulated service, unless such cross subsidy is provided for prevalence result from tariff regulation.

D. unjustifiable price discrimination: This refers to the situation that a telecommunications enterprise provides the same product or service to different trading counterparts or user groups at different prices or provides products or services of significantly different costs to various trading counterparts or user groups at the same price.

E. abuse of essential facilities: This refers to refuse to provide the essential facilities which are owned or controlled to its competitor or terminate the use of its competitor without any justifications, set an unreasonable price or trading terms, or provide essential facilities to other competitors at different prices or trading terms.

F. unjustifiable preference or discriminative treatment: When a telecommunications enterprise that supplies telecommunications services of intermediate input nature (such as interconnection services or circuit leasing) to itself, its affiliates and other competing telecommunications enterprises provides such services to itself and its affiliates at better prices or under more favorable trading terms than to its competitors without justifications.

G. unjustifiable long-term contracts or restriction on change of trading counterparts: When a monopolistic telecommunications enterprise establishes with its subscribers inappropriate long-term contracts whose clauses restrict the subscribers from changing trading counterparts or impose unreasonable penalties on subscribers terminating the contract to obstruct other telecommunications enterprises from competing with it on the market.

When filing a complaint that another monopolistic telecommunications enterprise is conducting vertical price squeeze under the above B, the complainant should provide information and evidences concerning the reasonable average costs for wholesale and retail of its products (services).

Price discrimination can be regarded as justifiable under the above D when it is adopted under the following circumstances:

A. adoption of average pricing for sake of service prevalence;

B. adoption of off-peak pricing to boost network utilization rates;

C. provision of combination rates, package rates or quantity discount rates;

D. adoption of Ramsey pricing to recover fixed costs or common costs;

E. adoption of price discrimination against intranet and inter-net services to reflect interconnection cost differences.

Example 3. How to determine anti-competition vertical price squeeze — imputation test

Suppose that Company A is a vertically integrated telecommunications enterprise that also provides wholesale services (for instance, unbundled local loop or Internet interconnection bandwidth) and retail services (for example, voice services or broadband connection) and it is the only supplier in the wholesale market while there are many competing operators in the downstream retail market. Company A provides services to the downstream competitors and itself at the price of NT$w per unit. In addition, its retail price and retail cost are respectively p and c. Is the wholesale price set at a level capable to drive the downstream competitors with equivalent efficiency out of the market? If the wholesale price is higher than the result of subtraction of the retail cost from the retail price, in other words $w>p-c$, the wholesale price will make the company's downstream competitors withdraw from the market because there is no profit for them. This, then, can be regarded a practice of vertical price squeeze. On the contrary, if the wholesale price of Company A does not exceed the result of subtraction of the retail cost from the retail price, in this case $w \leqq p-c$, then this does not constitute any vertical price squeeze. The adoption of the efficiency of a vertically integrated market leader as the assessment standard is called "Equally Efficient Operator (EEO) test." However, in cases where the market leader possesses competitive edges or essential facilities that its downstream competitors are unable to cope with, adoption of the "Reasonably Efficient Operator (REO) test" may be considered and the reasonable costs of the downstream competitors are referred to as the assessment criteria in order to promote effective competition in the downstream market.

Example 4　Differences in monthly subscription fees for residential and non-residential users

The local Internet companies set different monthly fees for residential and non-residential users. Generally, domestic users need to pay less monthly in-city network rent than non-residential users. Does this constitute an improper pricing behavior? Based on considerations of universal service and the lifeline characteristics of local calls, telecommunication regulators may require telecommunication enterprises to set lower rates for residential users who have greater non-commercial use and need greater flexibility. Non-residential users with a smaller demand elasticity charge higher rates. The pricing of this difference is based on the consideration of telecommunication policy, and the charging method that meets the principle of anti-demand elastic pricing should be considered as a differential pricing with justification.

Example 5. Are essential facilities only limited to physical telecommunications facilities?

The essential facilities doctrine originated in the case law of the US antitrust law. At present time, it has evolved into a principle with an abstract definition of multiple concepts. The term "facilities" is no longer limited to tangible conventional facilities such as railway bridges, power transmission lines or telecommunication networks. To the contrary, it has gradually evolved to include intangible services. In the telecommunications market, for instance, an essential facility may be a physical facility (such as a telecommunications network, piping, channel, manhole, utility pole or tower), space (such as a shared machine room, the telecommunications room in a building), or a service (such as billing service), a function (such as emergency call service), a capacity (such as submarine cable bandwidth access through a designated international route), or information (such as the SS7 signal system or database access). Generally speaking, the application of the essential facilities doctrine is employed in an ex post approach. FTC does not determine beforehand which telecommunications facility, service, function, capacity, or information is an essential facility. It will be determined only after a concrete case occurs and concerned parties have provided evidences to prove, in line with the aforesaid principle, that the concerned telecommunications facility, service, function, capacity or information constitutes/ or does not constitute an essential facility.

Example 6. Establishment of binding contracts by cell phone service providers with subscribers to compensate for cell phone price subsidies

To stimulate purchases, increase subscriptions and prevent subscribers from switching to other providers, cell phone service providers often promote sales by offering "cell phone plans" that allow consumers to buy cell phones at cheaper prices while the provider subsidizes for the price differences. However, the consumers are required to use the numbers provided by the provider for a certain period of time (the so-called "binding contract"). By doing so, cell phone service providers recover the subsidies from the monthly subscription fees and call charges consumers pay. Are such binding contracts inappropriate long-term contracts or do they constitute restrictions on change of trading counterparts? First of all, due to the intense competition on the cell phone service market, promotion by binding cell phone numbers with cell phones shall be considered as a normal way of market competition. Secondly ,despite that binding contracts do bar consumers from switching to other trading counterparts, if consumers are clearly aware of the contractual terms (such as use of a number from the provider, contract duration, rate scheme, and so on), they ought to be able to rationally judge whether they are willing to accept them. Therefore, FTC, at present, determines that such binding contracts to subsidized subscribers by cell phone service providers do not constitute inappropriate long-term contracts or restrictions on change of trading counterparts.

6. Mergers

Telecommunication enterprises' merger notification cases shall be reviewed under "Fair Trade Commission Disposal Directions (Guidelines) on Handling Merger Filings".

In addition to the provisions as set forth in the aforesaid Guidelines, the Commission may consider the following factors in reviewing the overall economic benefits:

A. the influence of the merger on improvement of production efficiency, allocation efficiency and dynamic efficiency;
B. whether the merger can help promote competition in the market in concern;
C. whether the merger can lead to provision of more comprehensive, more diverse, and better services;
D. whether the merger can help enhance international competitiveness.

7. Concerted Action

The Fair Trade Law regulates a concerted action by prohibiting it in principle but permitting it in exceptional instances. If practices of telecommunication enterprises fall within Article 14 of the Fair Trade Law and meets one of the provisos set forth under Paragraph 1, Article 15 of the Fair Trade Law, it is necessary to obtain a prior approval from the Commission for such concerted action.

If any one of the following conducts by a telecommunication enterprise with other competing telecommunication enterprises which would affect the market function of supply and demand of services, such conduct is considered in violation of Article 15 of the Fair Trade Law:

A. concertedly deciding product prices and service charges, or establishing contracts, agreements or consents to restrict each other from price adjustment or setting their own discount limits;
B. agreeing to set a limit on its production, productivity or facilities, or concertedly dividing the operating area and trading counterparts;
C. concertedly lowering the prices, formulating improper terms of transactions, refusing to supply or provide network interconnection or roaming service in order to eliminate or obstruct a third party from market competition;

D. disclosing to each other or exchanging important competition-sensitive information with regard to pricing, discounts, costs, R&D, subscriber information, etc.

Example 7. Types of agreement regarded as concerted pricing practices

In addition to concerted decision on product or service prices, the following types of agreement between telecommunications enterprises may also be regarded as concerted pricing:
(1) agreement on joint price increase or decrease;
(2) agreement on price calculation according to standard formulas;
(3) agreement on ways, limits and numbers of discounts to be given;
(4) agreement on charging rate according to announced criteria;
(5) agreement on pricing in accordance with the pricing of specific enterprises;
(6) agreement to notify one another of the time and range of price adjustment;
(7) Imposition of restrictions on the pricing or price adjustment of each enterprise through decisions of the trade union or association.

Example 8. Will network interconnection or roaming agreement be considered concerted action?

To ensure any-to-any connectivity between all telecommunications service subscribers and effective competition in the telecommunications market, the Telecommunications Act stipulates that Type I telecommunications enterprises have the obligation to provide network interconnection and, in order to do so, are required to negotiate with one another on certain issues such as sharing of interconnection cost, conveyance charges, collection of call charges and billing. Meanwhile, to overcome network coverage limits, cell phone service providers often establish roaming agreements with other providers to cooperate in the provision of mobile services. Will the aforesaid network interconnection or roaming agreements be considered concerted action? Generally speaking, as network interconnection and roaming agreements between telecommunications enterprises usually can stimulate competition and provide more convenient telecommunications services, they will

not be considered concerted action. However, if the parties involved in such agreements intentionally set high interconnection rates, conveyance charges or roaming charge splitting rates to restrict each other from price competition on call charges, or to divide the operating area or clientele through roaming agreements, it can be regarded illegal concerted action.

8. Boycott

When a telecommunications enterprise makes other enterprises in the upstream, downstream or relevant market stop supplying to or purchasing from a specific enterprise, and is likely to restrain competition, it may be in violation of Subparagraph 1 of Article 20 of the Fair Trade Law.

9. Discriminative Treatments

When a telecommunication enterprise provides the same services to counterparts of the same competition level at different prices, of different quality, at different discount rates or under unequal trading terms without any justifiable reasons, and is likely to restrain competition, it may be in violation of Subparagraph 2 of Article 20 of the Fair Trade Law.

10. Inducement with Low Price

When a telecommunications enterprise prevents any other enterprises from participating or engaging in market competition by disproportionate below-cost pricing or by any other improper means likely to restrain competition, it may be considered as being in violation of Subparagraph 3 of Article 20 of the Fair Trade Law.

11. Vertical Restraint of Trade

A telecommunications enterprise may be in violation of Article 19 or Subparagraph 5 of Article 20 of the Fair Trade Law when it provides telecommunications services for resale purposes to downstream resale businesses (such as wholesale for resale, bandwidth resale, payphone service resale, prepaid cards or phone cards) in cases of any of the following practices:

A. to impose restrictions on resale prices upon its downstream resale businesses without justifiable reasons;

B. to impose restrictions upon its trading counterparts or the operating areas of its trading counterparts without justifiable any reasons and is likely to restrain competition.

12. Unfair Competition Practices

When a telecommunications enterprise adopts false or misleading presentations or symbols that are sufficient to affect trading decisions with regard to its products or services in their advertisements or in any other ways to make it known to the public, it may be in violation of Article 21 of the Fair Trade Law.

A telecommunications enterprise competing for trading opportunities by means of offerings gifts or prizes that does not act in line with "Regulations Governing the Amount of Gifts and Prizes Offered by Businesses", may be in violation of Article 23 of the Fair Trade Law

13. Other Practices that are Sufficient affect Trading Order

A telecommunications enterprise deceives, conceals, or fails to disclose all necessary information during the trading process is considered deceptive or obviously unfair conduct, sufficient to affect trading order, and likely to be in violation of Article 25 of the Fair Trade Law.

14. The Policy Statements only serve as a general description of the characteristics of telecommunications enterprises and examples of practices that may be considered in violation of the Fair Trade Law. In every individual case, determination will be made in accordance with available evidences.