



# **Submission to Minister Billson on Competition Review Final Report**

## **Market Study Issue**

**May 2015**

### Introduction

The CCC welcomes the opportunity to comment on the issues raised in the Harper Panel's review of competition policy.

The CCC represents the interests of non-dominant telecommunications carriers with the sole purpose of promoting measures to improve the competitive environment.

For the purpose of this submission, the CCC wishes to reflect on the proposal in the panel report for the introduction of a market study power in Australia.

The CCC has previously proposed a process to require the ACCC to examine market conditions and outcomes on a regular basis as a discipline to ensure its regulatory processes in relation to access to bottleneck services are resulting in more competitive market conditions and internationally comparable prices, terms and conditions for consumers and business.

### The Issue of Urgency and Efficacy and a New Institution

The CCC strongly supports the introduction of a market study process to guide the administration of competition law. However, the CCC believes its introduction should be not subject to the creation of a separate institution, such as the proposal in the Harper review for the creation of an Australian Council for Competition Policy. It has two reasons for this:

- The urgency of the need for an improved process to assess market outcomes and impediments to effective competition in communications markets, and

- The importance of swift action to minimise damage to competition in the event that market studies find significant market power is being exercised.

The CCC believes these considerations outweigh the arguments that the introduction of a market studies process should wait and/or be dependent on the creation of a new competition policy institution.

With regard to the second point, the CCC is concerned that the decisions of the ACCC in its access and pricing deliberations have too often fallen far short of what is necessary to establish sustainably competitive markets in communications. This suggests an independent assessment of its stewardship of the interests of consumers and competition has merit. However, market studies conducted at arm's length from the competition regulator's decision making process could be of little practical use.

In addition, the CCC also believes arguments about inherent conflicts between the pricing and access functions and other market oversight functions have not been persuasively made out in the Harper review report.

It is clear proposals for radically changed institutional arrangements remain a medium term issue. There is, in the meantime, an urgent need for a market wide focus to be brought to bear in the administration of competition laws.

The CCC therefore believes a market study power should be implemented regardless of decisions about the more vexed/less clearly supported proposals around institutional reform, and that it should be integrated into market regulation and prices processes conducted by the ACCC.

#### Benefits of Integrating Market Studies with Remedies Powers

There are powerful arguments in favour of integrating a market studies focus with the functions of the competition regulator, as the panel notes has been done in dozens of other jurisdictions.

The CCC believes competition enforcement actions and market regulation must be informed by deep understanding of the overall market conditions that have given rise to concerns. It should also guide regulators in the choices they make as they seek to resolve observed problems.

The approach in the EU, for example, is designed to allow the regulator to apply remedies that are targeted and proportionate. Market studies identify markets where there are participants with significant market power, which in turn allows regulators to respond appropriately by choosing from a suite of available regulatory tools.

In this context, it is not clear to the CCC why the panel is keen to avoid an impression that a market study is a precursor to regulatory action.

If a market study unearthed evidence of market failure, this would naturally give rise to a community expectation that action to redress this would follow as a matter of course.

If there is no means to formally connect a market study finding of market dysfunction with processes to respond to these findings, introducing market studies would instead risk giving rise to greater frustration for competing businesses and consumers.

The CCC submits it would create unsustainable tensions if the ACCC was left to administer its regulatory functions on the same basis as today, while a separate agency was conducting market studies that demonstrated the regulation of competition was failing to deliver sustainably competitive markets.

It is likely the ACCC would regard the findings of an independent market study as something it was unable to take account of in discharging its duties under the CCA.

Indeed, if, as the Commission has repeatedly told the CCC and its members, the Commission considers industry structures irrelevant to its pricing and access deliberations today, the separation of consideration of markets to another body would seemingly underline to the Commission that it was expected to ignore market outcomes, and these should be exclusively policy matters.

It is not clear to the CCC what the Panel envisages as the mechanism to translate a finding of market failure to practical remedies. It implies a need for intervention by another authority, perhaps by the Parliament, where a market problem is found. This seems consistent with the panel's suggestion that the proposed Australian Council for Competition Policy would inform the broader debate on competition policy. (pg 454)

However, appropriate regulatory tools for dealing with the problems elucidated through a market study might already be available in the hands of the ACCC.

These might be more light-handed, quicker to implement and more efficacious than legislative responses.

The Panel argues that the ACCC has the ability to engage in market studies under Section 28 of the CCA.

However, in practice, the ACCC does not regularly conduct such reviews, and does not use them as a guide to its day-to-day regulatory processes.

### Communications Market Case Study

The Commission has not comprehensively examined the existing and future state of competition in communications markets since the so called Emerging Markets review in 2003.

In that study, which was prepared as advice to the Government, the ACCC recommended a series of measures to address vertical and horizontal market power arising through Telstra's ownership of access networks, and control of the dominant content provider, Foxtel. These were matters for legislators and it is important to note that the NBN policy was designed in large measure to address the vertical integration problem, while the Foxtel issue continues.

Meanwhile, the Commission does not exercise its pricing and access regulatory functions by reference to its own – albeit now dated – report findings. As discussed above, the Commission rejects suggestions from the industry that it should consider the very high market share and profit of Telstra compared with others in the industry and its international peers in these price setting processes.

The CCC submits that there is probably no clearer example than communications of a market that illustrates the need for the introduction of a market study approach to the application of competition law.

Communications markets are marked by constantly changing technologies. These technologies facilitate new entry but also allow incumbents to shift tactics in response to regulatory actions, challenging the ability of regulators to keep up. As discussed below, the ACCC's focus on regulating at the level of individual services has proven to be inadequate to respond.

The strong evidence is that, despite being the focus of constant regulatory action since 1997, communications markets are becoming less competitive and more concentrated on several crucial measures.

The result is that competition in communications markets again stands at a cross roads, even as the Government invests in the NBN to address some of the intractable structural barriers to competition.

The present approach to regulation of Australian communications services has exposed the inadequacy and inflexibility of the “bottom up” regulatory approach in operation today – that is, it focuses on identifying individual services that are found to be bottleneck inputs for particular retail markets, and become the subject of price and access regulation.

By contrast, as the CCC understands it, that the market studies approach utilised in the EU provides for a “top down” approach by regulators. The starting point is a determination as to whether a participant can be identified as having significant market power in a market.

If this is the case, regulation is focused on that source of SMP.

A top down view of Australian communications market demonstrates:

- deeply entrenched incumbency, as reflected in profitability and market shares on the part of Telstra, far beyond that of its international peers;
- severely constrained competition, as measured by stagnating market share and profit growth, and increasing concentration;
- high wholesale prices by comparison with other developed markets, and;
- fixed line services prices the highest or near highest in the OECD in almost all service categories measured.
- Lack of competing private sector investment in network and infrastructure of a kind seen in comparable developed economies.

There seems an obvious join-the-dots conclusion to be drawn from these data –

1. Telstra remains in a position to exercise market power;

2. it is doing so;
3. consumers are suffering uncompetitive prices and relatively poor quality of service as a consequence, and;
4. regulation has not been effective in curtailing Telstra's market power.

The ACCC has repeatedly told the competitive industry that it is unable to take this evidence of market-wide failure into account when it regulates on a bottom-up, service-by-service basis.

Rather, The CCC submits the bottom-up approach the Commission must take to setting prices for regulated prices has the effect of magnifying the problems that arise from significant market power and, it could be argued, create a vicious circle reinforcing that market power in the hands of incumbents.

The Commission processes rely heavily on data associated with specific services that is solely in the possession of Telstra. This means, in setting prices for individual services, the Commission depends on Telstra's willingness to volunteer data, or its own ability to extract from Telstra information about factors such as Telstra's costs and allocation of costs across different services classes and retailers, and Telstra's projections of future demand and costs.

Often, the models used to analyse these costs are themselves initially created by Telstra. Competitors, access seekers and consumers are reduced to seeking to understand and challenge the detail of the modelling at a progressed stage rather having an equal voice throughout the process.

This is a recipe for regulatory capture – Telstra and Commission staff engage regularly at a level of detail that creates little opportunity for other stakeholders to participate before the Commission is well advanced in determining its approach. There is little transparency for other stakeholders into these discussions and decisions between the Commission and Telstra. To their frustration, other stakeholders often find the basis on which a process will proceed has been determined in private discussions between Telstra and the Commission based on what data Telstra has agreed to provide.

In a process that took as its starting point an assessment of whether Significant Market Power is present in a market, evidence would be drawn from all stakeholders – including consumer bodies – on the experience of operating in the relevant markets, and the ACCC would be able to examine and take account of the evidence of overarching market outcomes, such as retail prices and market shares relative to benchmark competitive markets.

A regulatory regime that takes such a holistic assessment of the state of competition in economic markets should also be more effective in applying proportionate remedies. In the EU, these include structural measures to deal with the most serious and intractable problems.

Further, an approach based on the EU model would apply regulation only on participants found to have significant market power, meaning measures would be targeted only where they can have the greatest impact. Sources of market power that have not been addressed because, for example, they sit outside the list of already declared services and/or are inhibitors to competition because they are sold in retail bundles, would be identified and subject to action. It is also likely that a wider range of remedies than currently exists in Part XIB of the CCA would need to be available under the market study powers, including divestment powers.

The present regime has been inadequate to deal in an effective and timely manner with problems that the Commission has long identified but is seemingly unable to address. For example, as discussed above, the influence of exclusive content rights has been discussed by the Commission for more than a decade. There is yet to be a public examination by the Commission of the extent to which Telstra's internationally unique degree of horizontal integration, including content, has had an impact on the deplorable level of competition in communications markets today.