



INTERNATIONAL COMPETITION NETWORK

Advocacy Working Group

Report prepared by the subgroup n°3 : case studies

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1. PREFACE

The mandate of the Subgroup on Advocacy in Specific Sectors of the Advocacy Working Group of the ICN, as established at its first Annual Conference in Naples last year, was to undertake studies about advocacy efforts in specific regulated sectors in member countries with a focus on the principles involved, advocacy techniques employed, the role of the competition agency in those sectors, the interface between competition authorities and regulatory bodies, and the successes and failures of the advocacy efforts. It was suggested that the subgroup would invite ICN members to share their experiences in this field by submitting brief contributions on the sectors to be selected.

In order to maintain the work within manageable proportions, it was decided at an early stage to limit the scope of the efforts of the subgroup to the following four sectors: (i) telecommunications, (ii) energy, (iii) airline industry and (iv) legal professions. Early this year the agency that chaired the subgroup (France) sent out an invitation to members asking them to contribute on each of these sectors with a small paper setting out their experiences. Responses were received from eleven countries, some provided responses covering all four sectors while others responded to only some of them. The total number of contributions was 24.

The purpose of this report is to present the results of the exercise. Apart from this introduction it comprises a list of documents, a table classifying the contributions by sector and country and four sectoral chapters. Each chapter has an introductory section with an overview of the results of the country contributions and indicating the main sector-specific problems related with competition advocacy. After the introductory sections the full texts of the country contributions are included.

We wish to acknowledge the members who submitted contributions to the subgroup. We also acknowledge the work done by the authors of the introductory sections (United States Department of Justice, United States Federal Trade Commission, Romanian Competition Council and French General Directorate for Fair Trading, Consumer Affairs and Fraud Control) and express the hope that the report will be helpful also to members that did not directly participate, in shaping their advocacy activities in the sectors that were the subject of this study.

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2. COMPETITION AUTHORITIES SUBMISSIONS

COUNTRIES	Telecom.	Energy	Air Transport	Legal Professions
Armenia	x			
Australia		x		
France	x	x	x	x
Ireland	x		x	x
Japan	x	x		
Mexico	x	x	x	
Netherlands	x			
Romania	x			
Slovak Rep.	x	x		
Switzerland		x		x
United States	x	x	x	x

3. OVERVIEW OF ICN'S TELECOMMUNICATIONS SECTOR SUBMISSIONS

The ICN Competition Advocacy Subgroup received papers on advocacy in telecommunications from nine member countries: Armenia, France, Ireland, Japan, Mexico, the Netherlands, Romania, the Slovak Republic, and the United States. All describe telecommunications markets in transition from monopoly (whether governmental or privately-owned) to competitive. Although the development is slightly different in each country, the trend is uniform. Similarly, all describe the transition as explicitly informed by principles of competition. The following outlines the major themes presented in the telecommunications subgroup papers.

A. Industry Background and Transition

All nine papers describe wireline telecommunications markets as being in transition. Drivers of this transition appear to be technological developments, including wireless and data services, as well as advocacy of competitive principles by the relevant authorities.

For many years, France, Ireland, Mexico, Romania, and the Slovak Republic had state monopoly wireline providers that offered both local and long distance telecommunications services. Since the mid-1990s, those carriers have been privatized to some extent and the monopoly markets officially opened. The submissions recognize that opening a telecommunications market by law or regulation is merely the first step: the market may be open to competition officially and yet remain a monopoly for some period. The implementation of competition requires attention to details such as the prices and terms on which competitors can enter and obtain needed inputs from the incumbent. Thus, France, Ireland, Mexico, and Romania have established regulations that require incumbents to provide interconnection with new entrants. France, Romania and Mexico also have created a framework for establishing proper rates for interconnection services. On the other hand, while the Slovak Republic has opened its telecommunications market as of January 1, 2003, liberalization so far exists only on paper, as the Telecommunication Office has not yet exercised its regulatory powers notwithstanding the urging of the Antimonopoly Office. Japan, although it has not yet passed any formal legislation, has taken steps to create a regulatory framework for the telecommunications sector. These countries all have recognized that regulation is necessary to facilitate entry by new carriers and to prevent anticompetitive conduct by service providers that hold dominant positions in their respective markets.

In the United States, wireline telecommunications services were monopolized by a private company, AT&T, until 1984. That year, as a result of antitrust litigation by the Department of Justice, local service monopolies (the "Bell" companies) were spun off from AT&T, and the long distance market was opened to competition between AT&T, MCI, and other carriers. In 1995 the Federal Communications Commission ("FCC") declared that AT&T was no longer the dominant domestic long distance carrier. In 1996, Congress required the local telecommunications markets to be opened to competition, and included special provisions permitting the Bell companies to reenter the long distance market once they had proved that their local markets had been opened. Consistent with experience in other countries, formal and detailed regulations regarding prices, terms, and provisioning systems were necessary to open markets that had been officially and effectively closed to competition for decades. In addition,

some period of commercial use of the relevant systems has proved necessary in order to refine them so that what appears possible on paper becomes so in practice.

In contrast to the historical monopolies providing wireline telecommunications, U.S. wireless services were originally licensed and developed with at least two carriers in each geographic market. Wireless telecommunications have continued to be fairly competitive.

B. Competition Authorities

Seven of the responding countries have more than one governmental authority involved in telecommunications. In some countries, mandated changes in the structure of the industry were accompanied by changes in the structure of the government oversight. The Netherlands, for example, recently moved responsibility for telecommunications matters from the Ministry of Transport, Public Works, and Water Management to the Ministry of Economic Affairs. Ireland replaced the Office of Director of Telecommunications Regulation with the Commission for Communications Regulation. France and Romania created their Telecommunications Regulatory Authority to oversee the industry, including consulting with the Competition Counsel regarding basic rules of fair competition.

In other countries the relevant governmental authorities remained the same although their roles have shifted slightly. For instance, both the U.S. Department of Justice's Antitrust Division and the FCC retained responsibility for oversight of the telecommunications industry following the enactment of the Telecommunications Act of 1996. However, the Act shifted the authority to allow local monopoly carriers to reenter the long distance market from the U.S. District Court for the District of Columbia (which had retained the power to enforce and modify the antitrust settlement decree between the United States and AT&T, and to which the Department had submitted recommendations during the pendency of the decree) to the FCC, which must accord "substantial weight" to the Department's evaluation of each application.

In most countries, there appears to be a separation between the authority that regulates telecommunications and the one responsible for enforcing competition laws. The split is clear in the United States (the FCC regulates, the Department enforces), France (the Telecommunications Regulatory Authority regulates; the Competition Council enforces), Ireland (the Commission for Communications Regulations regulates, the Irish Competition Authority enforces), Mexico (Federal Telecommunications Commission; Federal Competition Commission), Romania (National Regulatory Authority for Communications regulates, the Competition Council enforces) and the Slovak Republic (Telecommunication Office regulates, the Antimonopoly Office enforces). Such compartmentalization provides the clearest basis for the need and execution of competitive advocacy as the competition authority seeks to ensure that the regulator takes into account competitive principles in overseeing the industry. The advocacy and input may be informal, as described by the Netherlands in its paper, or may include formal statements of position as reflected in the section 271 evaluations filed with the U.S. FCC by the Department of Justice. Such advocacy can be critical to encourage the regulator to ensure that the telecommunications markets are open to competition in practice and not merely on paper.

In some countries, such as France, Japan, Romania, and the Slovak Republic, the competition authority can itself impose remedies pursuant to the requirements of the competition law. Elsewhere the competition authority, such as the Irish Competition Authority and the U.S. Department of Justice Antitrust Division must request a court to impose sanctions for violations.

C. Examples of Competition Advocacy and Enforcement

Countries that have more than one governmental authority in charge of overseeing the telecommunications sector, such as France, Ireland, Romania and the Slovak Republic, have worked to increase cooperation between agencies to reduce duplicative enforcement activities and prevent inconsistent decisions. Some of the governmental authorities – those of the Netherlands for example – have carefully assessed market conditions before granting licenses to operators to ensure that they will not enhance a dominant carrier's position. In addition, France, Mexico, and Romania have substantially clarified the duties of incumbents to provide interconnection services while creating a cost-based price structure for the provision of such services.

Many of the responding countries have taken a hard stance against anticompetitive practices by dominant carriers through strict enforcement. The Irish Competition Authority, for example, has investigated many alleged anticompetitive practices and instigated proceedings to curtail abusive conduct by such carriers, including an incumbent's refusal to grant unbundled access to its networks and allegations of a price squeeze in the mobile-phone sector. Similarly, the Japan Fair Trade Commission, through the creation of a task force for the information technology sector, has zealously pursued enforcement, addressing issues such as vertical resale price maintenance of cellular phones and anticompetitive behavior in the DSL market.

Formal and informal advocacy by competition authorities also has a place in encouraging the development of more open markets. The importance of this has been recognized in the Netherlands and the United States by laws which require the telecommunications regulator to permit the competition authority to offer advice. In the United States the recommendation of the Department of Justice on a section 271 application by a local monopoly carrier must be accorded "substantial weight" by the FCC; the Department files formal, written evaluations on these applications. The Department recommended, and the FCC agreed, that the earliest section 271 applications be denied on the grounds that the applicants had not acted to open their local markets as required by the statute. This precedent led the local monopoly carriers to effect specific and concrete changes to prices, provisioning systems, and other terms and conditions, which permitted competitors to actually enter the legally-opened markets.

The competition authorities of France and the Slovak Republic regularly publish their decisions and issue statements regarding their positions on certain practices. The Antimonopoly Office of the Slovak Republic also issues notices of administrative proceedings, thereby allowing an opportunity for public comment on the proceedings, and has also entered into an agreement with the Telecommunications Office regarding coordination and cooperation on matters of common interest. The Irish Competition Authority raised concerns at the EU about the proposed system of relating significant market power obligations in telecommunications to competitive effects analysis and the impact it might have on the decisions of national Courts in competition cases. The Japan Fair Trade Commission has published guidelines on its position with respect to issues such as interconnection, the sharing of telecommunications facilities, and the provision of telecommunications services.

D. Conclusion

In sum, competition advocacy can be critically important in an industry such as telecommunications which is subject to regulatory oversight and is in transition from one paradigm (monopoly) to another (competition). Advocacy by competition authorities benefits the public interest by ensuring that competitive principles inform the industry's transition. The nine papers submitted describe concrete examples of these benefits such as the development of competition in France's long distance and mobile wireless markets and the concurrent fall in prices that consumers have experienced along with similar developments in Internet communications. Likewise, the United States has continued to develop competitive local telephony markets, and has increased competition in its mobile and long distance markets, which have led to greater consumer choice and reduced prices.

3.1. ARMENIA

The Commission has done relevant research concerning the legitimacy of the new procedure of Armentel CJSC, on connection of cellular phones enrolled since March 6 of the following year, based on different applications. According to the per-paid system connection packages the sale of SIMs was done only together with the telephones sold by Armentel. In the given case the customers were not only deprived of the alternatives to buying telephones, but also were forced to buy a relatively expensive one, when the same phones cost much less in other shops. The Commission discussed the above mentioned question on the Commission meeting, and assessed the activities of Armentel CJSC as a speculation of the latter's monopolistic role in the market of communications, thus a relevant decision was made. It was instructed to annul the alike procedure and simultaneously Armentel was forced to pay a fine of 5 million AMD.

It is important to note that this decision was appealed on the part of Armentel company, however the decisions passed by economic and cassation courts unanimously stated that the decision of the Commission was well argued and currently the plenipotentiary body is implementing the decision.

The research of the Commission done in the sphere of improper competition show that the most frequent are those violations which are qualified as misunderstanding around the economic subject or its activity and misleading of the population. There are many facts when the economic subjects use the brand and service marks of companies that are famous among the population for the production and sales of their goods. The Commission has undertaken measures to eliminate such phenomena from the market.

3.2. FRENCH MINISTRY OF FINANCE - DGCCRF

REGULATORY REFORM AND ADVOCACY IN THE TELECOMMUNICATIONS SECTOR

SUBMISSION TO THE ICN COMPETITION ADVOCACY SUBGROUP

Introduction

Competition advocacy refers to the activities conducted by competition authorities so as to promote a competitive environment by seeking to influence other governmental entities and increasing public awareness of the benefits of competition. In France, this role is carried out by both the Competition Council (Conseil de la concurrence) and the General Directorate for Competition, Consumers Affairs and Fraud Control ("DGCCRF").

The DGCCRF pursues these aims by discovering and analysing illegal agreements and abuses of dominant positions. It also examines mergers before proposing a decision to the Minister of Economy, Finance and Industry. Finally, it supports the opening up of regulated sectors such as air transport, telecommunications, energy and liberal professions to competition.

The *Conseil de la concurrence* pursues these aims by enforcing competition rules relating to cartels and abuses of dominant positions. It also gives its opinion on mergers when requested to do so by the Minister of Economy. The Council can also be referred to in order to provide its opinion on any question of competition by the Government, parliamentary committees, local authorities, professional organisations, trade-unions or consumers.

This paper focuses on the opening to competition of the telecommunications sector and the advocacy role of the regulators in France.

1- THE LIBERALISATION PROCESS

The French telecommunications sector has been considerably transformed over the last five years, changing from a monolithic and monopolistic market structure (fixed telephony) to a multiform and competitive sector (fixed telephony, mobile telephony, internet access).

At the outset, the theory of natural monopoly inspired the role of general government as responsible for operating telecommunications networks. This was perfectly understandable given that fixed costs were so high that only the State could afford to invest in, operate and regulate an activity that was viewed as a public service. And even in cases where a private company was running the service, monopoly was the rule rather than the exception.

Two main factors led the Government to give up this system of monopoly :

- firstly, technological progress that reduces fixed cost and allows the entrance of new players with real hopes for mid-term profitability;
- secondly, faith in competition benefits in order to improve global economic efficiency and global welfare for providers as for consumers

The French Telecommunications Act of 1996 dismantled the old monopoly system, entrusting the authorities in charge of regulation with the task of ensuring “*an effective and fair competition among network operators and telecommunications service providers, in the interest of users*”. In

the meantime, State authorities accepted a drastic change of their role, abandoning the direct administration of the network and concentrating on regulation stakes.

The regulatory role is currently shared by three institutions : the Telecommunications Regulatory Authority (ART), the telecommunications Minister and the Competition Council.

The liberalisation process has been conducted in three stages :

Stage one consisted in the legal separation of the operating and administrative functions. This was achieved by creating a company incorporated under ordinary law, in which the State still retains a majority interest.

Stage two consisted in abolishing monopoly and exclusive or special rights. This stage was accompanied by a series of measures aiming to preserve a high-quality service to users.

Stage three consisted in setting down legal rules designed to introduce competition to a market that remains dominated by the incumbent operator. These rules govern interconnection, licensing conditions for network and service operators, tariff monitoring and technical provisions enabling new entrants to pursue their business.

Establishing effective competition on the telephone market took time. Liberalisation is a gradual process and the incumbent operator must be willing to enter the competition game. During the first phase, newcomers needed to be able to enter the market thanks to regulator's and Competition Council's decisions entailing asymmetrical regulation on the incumbent.

2- THE ROLE OF REGULATORY AUTHORITIES

The role of each regulatory authority was very important to ensure the good processing of liberalisation. The Telecommunications Act fixed the frontier of the competencies.

The Telecommunications Regulatory Authority (ART) has some in-house competencies that allow it to safeguard the global economic equilibrium of the telecommunications sector : allocating frequencies and number (key resources), approving the incumbent interconnection tariffs, settling interconnection disputes and imposing sanctions if necessary.

ART shared some competencies with the telecommunications Minister who is in charge of allowing licenses to new entrants, establishing the cost of universal service and monitoring France Telecom's retail tariffs.

The Competition Council is keen on introducing basic rules of fair competition notwithstanding specific structures of telecommunications markets. The Telecommunications Act establishes cross-competencies with ART. Indeed, ART shall refer to the Competition Council any abuse of dominant position or any anti-competitive practice in the telecommunications sector. The ART and the Competition Council may seek reciprocal advice from each other on all matters within their jurisdiction and ART shall follow the opinion of the competition authority regarding the annual designation of the operators with significant market power (market share > 25% in value). Those operators are to respect ex-ante obligations in order to ensure the development of a competitive market.

3- TELECOMMUNICATIONS MARKET IN FRANCE

3-1 Fixed telephony market

During the period of public monopoly, the pricing of telecommunications calls was based on huge cross-subsidies, both between the various segments of market (network access and local communications vs long distance calls) and the various segments of users (business vs residential). The monopoly system was based on a huge discrepancy in pricing, with a very low pricing of network access compensated by a high fare for long distance calls. This system allowed an extensive coverage of the national territory with costly investments throughout remote areas. Access to the network was granted at a reasonable price for all the consumers, located in Paris or in a remote village of Brittany. As a consequence, the stress put on global social welfare hinders the system from reaching economic efficiency. Massive financial transfers between users of international services and local users made the system work but the lack of transparency led the sector far from the economic optimum.

The opening of markets in 1998 led to a new system of prices based mainly on real costs. New comers chose to enter the profitable segment of long distance calls and the fall of prices on this segment due to competition led the incumbent operator to raise the pricing of network access. As a consequence, an appropriate pricing of network access allowed new comers to operate successfully in the local loop market.

The available data on prices show that the monthly retail access network price increased from 7 € in 1995 to 13 € in 2002. In the meantime, the communications prices have been roughly divided by two. The telephone bill decreased by an average 30 % for business customers and by an average 10 % for residential customers. But there are winners and losers within residential customers. People consuming few communications have to fully support the raise of line rental without substantial benefits in communications. On the contrary, people consuming a lot of communications have a different structure of their telephone bill with a smaller part devoted to the line rental.

Nevertheless, the concept of universal service has been introduced in order to ensure the provision of a quality telephone service at an affordable price.

France Telecom is responsible for the provision of the universal service which includes the network access service, local and long distance calls, public pay phones, phone directory and emergency calls free of charge.

The universal service does not involve competition distortions as the net cost burden is shared by all operators either they have many universal service users or not.

3-2 Mobile telephony market

The introduction of competition rules to the mobile market has undoubtedly fostered fast development and unprecedented growth in the number of mobile services users. Between 1994 and 2002, the customer base increased from 1 million to 38 million, which means that it virtually doubled every year. This growth, shared between three operators, was accompanied by a huge increase of volumes and a strong fall in prices parallel to the decrease of the monthly average revenue per user, evolving from about 85 € (excl. VAT) in 1994 to 40€ in 2002.

The quality of service issue is a very important matter of regulation on the mobile market. Each year, a quality of service inquiry is conducted by the regulatory authority. The aim of this inquiry is to ensure that mobile operators achieved their regulatory obligations relative to geographic coverage of the territory and to ensure the rating operators. The results are considered to be

competitive incentive and give the first operator (global quality of service, urban and rural areas, in-doors quality...) a good premium on the market.

The mobile market example illustrates that competition rules are not contradictory with quality of service as soon as an independent regulator ensures the monitoring of homogeneous parameters and the rating of operators.

For example, the regulatory interventions allowed the provision of transparent billing information to users. Today, the Government is obtaining the provision of mobile services on a national basis with the coverage of the entire metropolitan territory.

3-3 Internet telecommunications services

Internet also experienced a huge growth over the past three years. Traffic has doubled between 1998 and 2001. In the last two years, prices for Internet access have decreased by an average 60 %, ranging from 50 % up to 75 % depending on different kinds of pricing formulas. The main stakes now lie in the unbundling of the local loop which is necessary to strengthen competition in high-speed internet traffic. ADSL technology is now available and delivers reasonable hopes for a rapid development of the high-speed market. The incumbent operator took strong advantage of being the unique operator owning reserved phone lines to connect ADSL. But all Internet access providers should now be allowed to propose ADSL connection without competition disadvantage. Indeed, ART and the Competition Council made very important decisions in order to force France Telecom to give an access to its network on a cost-oriented base and let other competitors order quickly and freely ADSL access thanks to an Extranet server.

4- ADDITIONAL ADVOCACY RELATING TO PROCEDURES AND COMMUNICATION

The mere publication of letters of the ministry of Finance (concentrations) and decisions of the Competition Council, Court of Appeal and Cour de Cassation in the Official Bulletin of DGCCRF (with access via the Internet) contributes to competition policy's knowledge of the specialized (or unspecialized) public. Moreover, most famous cases are often commented on in the press or other media, and the theme of competition in the telecoms sector is very popular due to the large diffusion of fixed and mobile telephony, and related appliances.

In addition, DGCCRF officials participate in the procedure before the Competition Council, not only as far as investigations are concerned, but also at the ultimate stage, when the government commissioner (a DGCCRF member) exposes the facts, and advocates the opportunity of imposing fines or granting interim measures.

5- ADVOCACY PROSPECTS

France today enjoys significant experience concerning competition in telecommunications. France represents one of the most significant markets in Europe and the liberalisation process has borne its fruit : a drop of prices for all consumers and the development of new services.

In the telecommunications sector, opening to competition should not be opposed to the traditional idea of "Public service". The liberalization process for telecommunications proved the possibility to maintain a high standard of service to individual consumers with liberalization, and even to increase this standard on many points. Quality is better, and price is lower. Such results are mainly due to the competitive pressure that gives the operators strong incentives to lower the

production costs and to design new products. In a sense, such a competitive pressure probably is the best of regulators.

A new European regulatory framework recently enacted will strengthen competition in the next few years. This framework creates special duties for so-called operators proved to have a significant market power. These operators are under close control concerning their pricing policy for retail as for interconnection markets. As a consequence, the action of national regulatory authorities throughout the European Union will be under close supervision considering that the common law of dominant position and competition rules will apply more and more in the specific field of electronic communications economy. A new approach is currently experienced that is based much more on free competition rather than on a regulatory scheme. The strategic role of the fixed telephony network is no longer alive for international calls, data transmission markets and also for the local loop. And all the operators -small-size, medium-size or major companies- should fairly compete in order to deliver best services at a low price with satisfactory profitability in all the segments of the telecommunications markets.

In conclusion, the new European framework, which shall be transposed on 24 July 2003 strict deadline, sets the principle of an evolution of sectoral authorities' role and an enhancement of competition authorities' role.

A recent decision of the Conseil de la concurrence is particularly relevant in this regard. Future development of Internet access market essentially depends on *France Télécom* which uses, on its traditional network, ADSL technology. To propose their services, Internet Service Providers (ISP) need to know from *France Télécom* whether a telephone line is consistent with ADSL equipment and what type of modem they have to choose.

Further to a complaint from ISP *T-OnLine*, the Conseil noted that *France Télécom* might grant privileged and discriminatory conditions to its subsidiary *Wanadoo-Interactive*, including through its network of commercial agencies. It therefore asked *France Télécom* to stop marketing its *Wanadoo* packs *Extense* until all ISP had sufficient information, in view of eliminating any competition distortion. The Paris Court of Appeal confirmed this interim measures decision on 9 April 2002.

3.3. IRISH COMPETITION AUTHORITY

INTRODUCTION

This note is a response to a request for input from the ICN's Case Studies subgroup no 3. The role of the Irish Competition Authority (CA) may differ from that of many other ICN members, for example, regarding the amount of information we may legally provide to the Subgroup in relation to our enforcement activity. In providing the information requested, the Authority has taken into account the confidentiality provisions of the Competition Act 2002.

THE COMPETITION AUTHORITY 'S ENFORCEMENT AND ADVOCACY ROLE

The CA's Enforcement Powers

While the competition authorities of many other countries can impose administrative sanctions for breaches of the competition law, this is not the case in Ireland. Because of the separation of powers doctrine enshrined in the Irish Constitution, the Irish Competition Authority is not empowered to impose such sanctions directly. Rather, the Authority's function is to investigate and take cases in the courts against undertakings or individuals that it believes are in breach of the Act.¹

The Authority does not itself make determinations or impose fines. When the Authority's investigation into a complaint or practice is completed, it may decide to take enforcement action, whereupon the matter is *sub judice* and the Authority is largely precluded from public comment on the issue until the courts have heard the case. If the Authority decides not to take enforcement action on foot of a complaint, the practice is simply to write to the complainant stating its decision, without giving reasons. This is because anyone aggrieved by an anti-competitive agreement, decision or concerted practice, or an abuse of dominance, has a right of private action in the courts under Section 14 of the Competition Act, 2002. Any stated reason by the Competition Authority for not taking action (for example, that it did not consider the behaviour to be abusive, or that insufficient evidence existed) might deter an individual from taking such action where it might otherwise be warranted. The Authority does, in some cases, include a brief summary of the matter in its Annual Report, where the case is of sufficient interest.

IT IS OF NOTE THAT IF A FIRM WAS FOUND TO HAVE ABUSED ITS DOMINANCE, THE AUTHORITY CAN SEEK REMEDIES FROM THE COURT. UNDER SECTION 14 (7) OF THE NEW ACT, THE COURT CAN:

- (a) require the dominant position to be discontinued unless conditions specified in the order are complied with, or
- (b) require the adjustment of the dominant position, in a manner and within a period specified in the order, by a sale of assets or otherwise as the Court may specify".

¹ These cases may be taken in the High Court for breaches of both Section 4 (anti-competitive agreements, decisions and concerted practices) and Section 5 (abuse of dominant position), and in the Circuit Court for breaches of Section 5 only. The new Competition Act has strengthened the enforcement provisions introduced in the 1996 Competition (Amendment) Act while the prohibitions remained unchanged.

The 2002 Act's Confidentiality Requirements and their Exceptions

The Authority takes into account the confidentiality provisions of section 32 of the Competition Act 2002. Exceptions to these requirements include exchange of information between the Authority and either a statutory body who is party to a cooperation agreement or a “foreign competition body²”.

Consequently, the information that the Authority can provide, to the ICN or in any other public forum, is limited both by the requirement not to prejudice possible court action (taken either by itself or by an aggrieved party) and by the confidentiality provisions of the Act. Within these constraints, however, we have tried to provide the fullest possible information.

ADVOCACY IN THE TELECOMMUNICATION INDUSTRY

The Competition Authority

The CA has a function to advocate for competition across the whole of the economy under Section 30 (1) of the Competition Act, 2002. The Act stipulates that it is the Authority function:

- (a) to study and analyse any practice or method of competition affecting the supply and distribution of goods or the provision of services or any other matter relating to competition (which may consist of, or include, a study or analysis of any development outside the State);
- (b) to carry out an investigation, either on its own initiative or in response to a complaint made to it by any person, into any breach of this Act that may be occurring or has occurred;
- (c) to advise the Government, Ministers of the Government and Ministers of State concerning the implications for competition in markets for goods and services of proposals for legislation (including any instruments to be made under any enactment);
- (d) to publish notices containing practical guidance as to how the provisions of this Act may be complied with;
- (e) to advise authorities generally on issues concerning competition which may arise in the performance of their functions;
- (f) to identify and comment on constraints imposed by any enactment or administrative practice on the operation of competition in the economy;
- (g) to carry on such activities as it considers appropriate so as to inform the public about issues concerning competition.

With respect to the communications sector, a number of issues were examined in 2002. In March, the Authority raised concerns at EU level about the proposed system of relating significant market power (SMP) obligations in telecom to competitive effects analysis and the impact that this might have on the decisions of national Courts in competition cases. The Authority was pleased that its concerns were taken on board in the final Recommendation³.

² Defined as “person in whom there are vested functions under the law of another state with respect to the enforcement or the administration of provisions of that state’s law concerning competition between undertakings (whether in a particular sector of that state’s economy or throughout the economy generally)”

³ Commission Recommendation of 11/02/2003 on Relevant Product and Service Markets within the electronic communication sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC if the European

The Commission for Communications Regulations

The Communications Act, 2002⁴ sets, as one of the objectives for the Commission for Communications Regulations (ComReg), the promotion of competition. The Commission replaced the Office of the Director of Telecommunications Regulations (ODTR). Further details of this, and ComReg's other objectives, are available on its website (www.comreg.ie).

Pursuant to section 34 of the Act, the Authority entered into co-operation agreement with the Commission in December 2002. The agreement formalised the existing informal relationship between the two organisations, facilitating co-operation and avoiding duplication of activities. The agreement also aims to ensure consistency in decision-making. Practically, the agreement includes provisions on exchange of information, forbearance of performance of functions by one party where the other is already performing similar functions in relation to a matter, and on consultation.

Prior to signing the agreement, the Authority's Advocacy Division drafted, with the ODTR, a Joint Response to the European Commission Consultation on Relevant Product and Service Markets within the Electronic Communications Sector⁵. The joint response highlighted a number of concerns with regard to the implementation of the recommendation.

The Minister for Marine, Communications and Natural Resources

Under the old legislation, the ODTR was a completely independent body. Under the new Communications Act, 2002, the Minister for Communications has the power to issue policy directives. The Minister has indicated that he will issue a policy directive to ComReg to order telecom firms to offer flat-rate internet access services.

THE INDUSTRY

Background: the Market Liberalisation

Liberalisation has occurred at all levels of the vertical chain in Irish telecommunications sector. Although there has been some alternative provision of value added services since 1992, liberalisation largely began in 1997 with the provision that alternative infrastructure providers could enter the market and compete with Telecom Eireann with some derogations. The establishment of an independent regulator and the privatisation of the State owned monopolist were key landmarks in the liberalisation process.

The Derogations

In 1996, the EC decided to complete the liberalisation of the telecommunications market in member states by January 1998 but allowed some member states, including Ireland, to apply for derogations. Ireland sought and was granted the following derogations:

- full liberalisation of voice telephony and the associated public telecommunications networks by 1 January 2000;

Parliament and of the Council on a common regulatory framework for electronic communication networks and services.

⁴ http://www.comreg.ie/_fileupload/publications/Act20of2002.pdf

⁵ www.tca.ie see submission: S/02/003

- international interconnection of mobile telephony networks by 1 January 1999; and
- provision of alternative infrastructure for liberalised services by 1 July 1997.

Further liberalisation took place in 1997 with the adoption by the Minister for Public Enterprise of regulations dealing with:

- alternative infrastructure provision,
- removal of monopoly on provision of satellite-based telecommunications services, and
- the supply of liberalised telecommunications services over cable TV networks.

In 1998, the Interconnection, Licensing and Leased Lines Directives were all transposed into national law.

The Minister made the decision in May of 1998 to end the derogations early and to introduce competition from 1 December 1998. The decision to end the liberalisation derogations was largely driven by the fact that telecommunications is a necessary input to the world class, high-tech industrial base that Ireland has succeeded in attracting. Ireland had engaged in a huge effort to upgrade its telecommunications infrastructure (through digitalisation) during the 1980s. The necessary regulations were adopted to allow these derogations to end.

The Establishment of an Independent Regulator

Regulation was separated from ownership with the establishment of the Office of the Director of Telecommunications Regulation under the Telecommunications (Miscellaneous Provisions) Act, 1996. The Office was to implement the policy agenda of regulatory reform and liberalisation of the sector. Independent regulation was to enable both domestic and overseas firms to compete on a level playing field in the Irish telecommunications market. The new institutional framework also aimed at making regulation more explicit and transparent.

Privatisation of the Former State Owned Monopolist

Telecom Eireann, the State owned monopolist was privatised in 1999 (hence the name change to *eircom*) in the form of a public share offering. *eircom* remains a vertically integrated company. In 2001 *eircom* decided to sell Eircell, Ireland's largest mobile phone network and service provider to Vodafone.

Until it was privatised, Telecom Eireann held 75% ownership of Dublin's local monopoly cable TV network and service provider (Cablelink). After its privatisation, the Government obliged *Eircom* to sell its stake in Cablelink.

THE MARKET PLAYERS

Telephone Services

Voice telephony was fully liberalised on the 1 December 1998. Accompanying this, the legal and regulatory conditions for access to *eircom*'s network by firms competing downstream markets were clarified. A licensing regime was introduced to act as a screening device to ensure that entrants satisfy minimum efficiency and quality standards. The existence of 86 licence holders⁶ indicates the potential for effective competition to develop in the market.

⁶ ComReg Document 02/106b - Quarterly Key Data available on ComReg's website <http://www.comreg.ie>

Fixed Line and Mobile Market

The revenues generated by the fixed lines represent 60% of total telecommunications markets in 2002. The market share of other Licensed Operators' (other than *eircom*) was approximately 21% of the fixed line market. At the end of 2002, the mobile penetration rate was 77% with approximately 3 million mobile subscribers. The market share of the mobile operators was the following: Vodafone (formerly Eircell) had 57%, O2 (ex Esat/Digiphone) 40% and Meteor, had 3% market shares at the end of 2002 (Meteor's licence was awarded in January 2001 after lengthy court proceedings). Meteor's growth and the imminent entry of third generation operator, Hutchison Whampoa, are expected to offer further choice and innovation.

Data Traffic and Internet Access

Residential internet penetration is estimated at 51%. PSTN is the predominant form of home internet access (91%) followed by ISDN (6%). Between residential and commercial lines, there are approximately 345,000 ISDN access channels. There are approximately 22,000 retail leased lines circuits (95 % of the circuits are under 2 Mbits) and 8,000 wholesale leased lines.

Local loop unbundling

Local loop unbundling has been very slow. Ireland has the highest monthly rental price for unbundling in Europe and an above average price for connection. However, price reductions are expected decline with Esat BT's recent roll out of DSL (Digital Subscriber Line) and via new entry in the market.

ComReg is to relax the rules for wireless operators in an attempt to spur competition in the broadband market. ComReg also plans to issue new-style licences from next month. It is hoped that this will provide a more stable framework for firms operating in the fixed wireless access market.

Cable and/or satellite television service

Nearly 585,000 households with cable/MMDS subscribe to basic services in Ireland. Approximately 9% of them have upgraded to digital. In addition, BSkyB has 255,000 subscribers. Two operators share the rest of the market.

SELECTED ISSUES INVESTIGATED BY THE CA

Provision of Telecommunications Infrastructure

In 1999 the Authority received a complaint relating to an agreement between a telecom operator and the CIE Group, the owner of the national state monopoly railway company. Under the agreement CIE would lay the operator's cables along its tracks in return for consideration (including access to capacity on the cables). The complainant argued that CIÉ controlled nationwide wayleave rights and that, consequently, it was in a unique position from the point of view of a network operator which wished to achieve rollout of a national network in as short a time. While, theoretically, other infrastructures were also available, these were not equivalent to CIÉ's since their owners could not grant wayleave rights and since the Esat/CIÉ telecommunications

network, unlike others, was substantially in place. The complainant argued that CIE was in a dominant position in the provision of telecommunications infrastructure in Ireland. The complainant argued that CIÉ's effective refusal to negotiate for the use of its cable network was an abuse of its dominant position

The arrangements between CIÉ, Esat and Iarnród Éireann, which were the subject of this complaint, were also notified both to the Commission and to the Authority. Under the Competition Act, 1996, when an agreement was notified to the Authority, the Authority had to decide whether to issue a certificate stating that, in its opinion, on the basis of the facts in its possession, the notified agreement did not contravene Section 4(1) of the Competition Act, 1991. If the agreement did contravene Section 4(1), the Authority could nevertheless grant a licence under Section 4(2) of the Competition Act to the agreement provided that certain conditions were met. These provisions were the equivalent in domestic law of Articles 81(1) and 81(3) of the EU Treaty.

In its Decision No. 577 of 28 January 2000⁷ (see Appendix II), the Authority issued a certificate to the agreement (i.e. found that it was not restrictive of competition) after it had been modified to reduce the period of exclusivity during which other operators could not sign a deal with CIE. The reasoning followed that of the Commission in the Telecom Development case.

Under the Competition Act, 1996, the Authority had no power to certify whether or not an agreement breaches Section 5, nor to licence any breach of Section 5. Nevertheless the Authority's decision on the notified agreement concluded that access to CIÉ/Iarnród Éireann's property in order to lay cable could not be regarded as an essential facility.

LOCAL LOOP

In the latter part of 1998 the Authority informed Telecom Eireann (subsequently *eircom*) that unless certain practices, concerning access to the local loop, were terminated proceedings would be instituted under Section 6 of the Competition Act 1996. Following a refusal by Telecom to discontinue the behaviour involved, the Authority issued proceedings in April 1999 alleging that Telecom Eireann's refusal to grant unbundled access to the local loop constituted an abuse of a dominant position contrary to Section 5 of the 1991 Act.

However, in subsequent developments Regulation 2887/2000 of the European Parliament and of the Council on unbundled access to the local loop ('the LLU Regulation') required *eircom* to publish from 31st December 2000, and keep updated, a reference offer for unbundled access to their local loops and related facilities. Charges were to be set on the basis of cost orientation. Additionally, Article 3(2) of the LLU Regulation required *eircom*, from 31st December 2000, to meet reasonable requests from beneficiaries for unbundled access to their local loops and related facilities under transparent, fair and non-discriminatory conditions. Requests may only be refused on the basis of objective criteria, relating to technical feasibility or the need to maintain network integrity. As a result of these developments the court action was settled and the case closed.

⁷ www.tca.ie, see Decision No 577 of January relating to Notification No. CA/8/98 - Esat Telecommunications Ltd./CIÉ/ Iarnród Éireann - non-exclusive licence to lay cables.

LENGTH OF MOBILE CONTRACT⁸

In 1996 the Authority received a complaint concerning Eircell's inclusion in its standard rental terms of a provision that customers were obliged to pay a minimum of 12 months' rental. This, it was alleged, was designed to prevent customers switching to Esat Digifone, a new entrant, which had been granted a licence by the Government to provide a second mobile telephone service throughout the State.

On the basis of Esat's projections of the likely development of the market over the next five years, it appeared to the Authority that a large part of the potential market was still open to Esat. In addition, even customers who had a one-year tie to Eircell were not prevented from switching to Esat for a full year following its launch as the agreements had already started prior to the launch. The Authority took the view that while Eircell was certainly trying to retain customers in expectation of the entry of a new competitor, this was a rational business response, and it did not appear that the number or period of time for which customers were committed was such that it would prevent Esat from entering the market.

The Authority took the view that it would not take further action on foot of the complaint at the time and informed the complainant accordingly. Therefore, the Authority found no abuse of dominance.

RETAILERS OF MOBILEPHONES

Provision of Airtime

The complainants alleged that a mobile phone company was abusing its dominant position in the mobile telephony market by subsidising its own sales arms to a greater extent than independent agents. Mobile operators distribute their products through their own direct sales arms and through agency agreements with independent retailers. It appears that subsidising the price of the handsets is a long-standing practice in mobile phone retailing. Various complaints alleged that the mobile phone company was "poaching" customers from agents by bypassing them and offering better deals through their own sales organisations.

In considering this matter, the Authority noted that the law as then interpreted by the courts did not require operators to provide wholesale airtime to anyone other than a licensed operator. This prevented independent service providers and retailers from becoming a source of competition in the mobile market. While cross-subsidising mobile phones might impact on the profitability of independent retailers, the customer would benefit in terms of lower mobile phone costs. The retailers, who were not prevented from becoming dealers of competing operators, nor from selling the products of competing operators simultaneously, freely entered into agency agreements. While the actions of the operators might be "squeezing" the margins of retailers, the indications were that this represented operators competing aggressively for network connections, albeit through the subsidisation of mobile phones rather than through usage rates. The net result was that consumers benefited.

⁸ Source: Competition Authority Annual Report, 1996

Retailers Wholesale Margins

In August 2002, the Authority received 30 complaints from individual retailers and representative bodies in relation to Vodafone's pre-paid mobile phones. It was claimed that Vodafone's reduction in wholesale margins to service providers on €10 and €15 electronic top ups squeezed retailer margins unfairly. They alleged that Vodafone's behaviour was an abuse of dominance, which constituted a breach of the 2002 Act. Vodafone's reduction of the wholesale margin on €10 and €15 top ups resulted in some retailers charging a handling fee to consumers on these denominations⁹.

It was established that the facts did not support a conclusion of abuse of dominance. Several factors were considered in reaching a determination in this case, *inter alia*: many retailers chose not to charge a handling fee. Top-up credit can be bought online, by text or by phone, at ATM machines and through numerous outlets without any handling fee being levied, the retailer margins on €20 plus were left unchanged and sales of Vodafone top-up grew by 60% in the financial year ended 30 April 2002. In addition, Vodafone stated that the cost savings affected through the reduction in wholesale margins would be ploughed back into its business to increase the services and products to consumers.

Although it was felt that no breach of the Act had taken place in this case the situation will be monitored to ensure compliance with the 2002 Act.

THE ACTIONS TAKEN BY PRIVATE PARTIES: MERIDIAN COMMUNICATIONS LIMITED AND CELLULAR THREE LIMITED-V-EIRCELL LIMITED

This paper closes by looking at an important recent decision that has been made in relation to issues of dominance in the mobile sector.

In July 1999 Meridian Communications Limited and its subsidiary Cellular Three Limited applied for a number of orders against Eircell, including one restraining it from terminating a volume discount agreement with Meridian. The Court refused the injunction on the grounds that Meridian was required to have a licence to offer mobile telephony services to the public. The decision was appealed to the Supreme Court, which declined to adjudicate and instead directed that the case should have an early trial. The case commenced on the 18th January 2000 and was heard by Mr. Justice Higgins. In his decision of the 4th April Mr. Justice Higgins decided that Meridian did not need a licence for their business, and also that Eircell were not obliged to renew the a volume discount agreement with Meridian. However, at the close of the trial Mr. Justice Higgins was also asked to rule on two additional issues: (i) whether Eircell was jointly dominant with the other operator in the market (Digifone); and (ii) whether Eircell was dominant on its own.

Joint Dominance

On the 4 October 2000 Mr. Justice Higgins ruled that Eircell were not jointly dominant in the market:

⁹ The Irish Retail Newsagents Association (IRNA) distributed notices to its members which stated that certain handling charges were to be levied on €10 and €15 e top-ups. The Authority advised the IRNA that this appeared to be a breach of the Act, albeit unintentional. The IRNA informed its members they should set prices individually and the notices circulated by the IRNA should be withdrawn from display

“In my view there is no prima facie evidence of a joint dominance as required in the legal sense. Even if one accepts that the structure of the market is sufficient to infer economic links, there has been no evidence that the parties in the present case adopt uniform conduct, or the same conduct on the market.

The Plaintiffs submit that I can infer that the joint conduct consists in pricing above the competitive price. In my view that is not sufficient. Indeed the concept of ‘conscious parallelism’, seems to be fundamentally different to the concept of acting as a unit or as one in the market place, which is a requirement for joint dominance. The uncontradicted evidence is moreover that there is a level of competition between Eircell and Digifone.”
[Judgment 4.10.00, p22]

Just before stating this conclusion Mr. Justice O’Higgins had said that Meridian relied on the EU’s *Access Notice* on Telecommunications (para 79). This said that the European Commission did not consider that either economic theory or European law implied that explicit agreements were

“legally necessary for a joint dominant position to exist. It is a sufficient economic link if there is the kind of interdependence which often comes about in oligopolistic situations.”

Also, the Judge said, Meridian relied on the decision of the European Court of First Instance in *Gencor v Commission* [case T-102/96] in which the court had said [paras 273-6] that;

...“there is no reason whatsoever in legal or economic terms to exclude from the notion of economic links the relationship of interdependence existing between the parties to a tight oligopoly...”

However, the judge went on, according to Mr. Paul Sreenan SC (for Eircell) the *Gencor* case was “a classic merger analysis” and

“was therefore an *ex ante* analysis, in contrast with the decisions in courts in relation to breaches of Article 86 [now 82] of the Treaty. He submits that the case is not authority for the proposition that the possibility of tacit collusion is sufficient, to establish joint dominance, but merely states that from the merger point of view it is legitimate for the regulatory authority to use the mergers regulations to prevent it happening prospectively.”

The judge said: “It is the plaintiffs’ case that joint dominance is equated with tacit collusion.” He then quoted, from the transcript, a passage in which Meridian’s economist said that he could not accept that proposition. The judge then gave his decision on dominance.

Dominance

On the 5th of April 2001 Mr. Justice Higgins ruled that Eircell was not dominant on their own in the market:

“Taking into account all the evidence in the case the Court is not convinced that Eircell can act to an appreciable extent independently of its competitors and ultimately of consumers. The plaintiffs have failed to prove on the balance of probabilities that Eircell are dominant. It follows that any claims based on the abuse of dominance and hence breach of Section 5 of the 1991 Competition Act must fail. [Judgment 5.4.01, p66]

On the issues of Eircell's high market share (60%), the small number of competitors, barriers to entry and barriers to expansion Mr. Justice Higgins said:

“ The high market share of Eircell, the low number of competitors, the high barriers to entry are all factors which would tend to indicate its dominance in the market place. However, when examined in the context of this particular case, the position appears to me to be different. The significance of the high market share is greatly diminished having regard to the rapid decline in the market share in a relatively short period. The importance to be attached to the small number of competitors is significantly reduced by (a) consideration of the regulatory regime, which is the background to the market (b) by the size and strength of the competitor and (c) in light of the knowledge that new licenses are to be awarded. The high barriers to entry as a factor pointing towards dominance must be looked at in the context of the low barriers to expansion, which are characteristic of the market with which we are concerned herein. In that context the weight to be attached to high barriers to entry as an indicator of dominance is much reduced.” [Judgment 5.4.01, p24]

On the evidence of Eircell's alleged high prices:

“The analysis of the various reports and data produced or referred to in the evidence is inclusive and unsatisfactory.” [Judgment 5.4.01, p44] (p.44)

Moreover the Judge found that,

...“Even were it accepted that Irish mobile telephony charges are high, it is difficult to know what significance should be attached to that, because of the many different possible reasons for such price which Professor Cave at p.50 of his report called “*a host of factors that are unrelated to competition*”.” [Judgment 5.4.01, p45]

CONCLUSION

To date, the main Irish competition law case remains the Meridian case. It provided case law on dominance and joint dominance. The case showed some of the difficulties associated with competition law enforcement: it is time consuming and expensive. In a fast moving industry like telecommunications, this feature highlights the critical role of the national regulator.

The local loop case was settled following the introduction of the EU regulation on unbundled access to the local loop. In retrospect, cases such as the one initiated in Ireland probably helped create a momentum for the fast introduction of the regulation. The investigation of the case also showed that co-operation between the Authority and, the ODTR, then, would benefit from being formalised.

The Competition Act, 2002 provided formal grounds for co-operation with sectoral regulators. These agreements cover the sharing of information, forbearance and measures to eliminate duplication. The agreement with the Commission of Communications Regulation was signed in December.

3.4. THE JAPAN FAIR TRADE COMMISSION

Approach to Regulatory Reform in the Telecommunications Sector

1. Approach to System Reform

The Japan Fair Trade Commission (hereinafter “JFTC”) has studied how to promote fair and free competition in the telecommunications sector at the Study Group on Government Regulations and Competition Policy. This group has already submitted a series of proposals and has recently studied measures to promote fair and free competition in the telecommunications sector where the market structure has changed rapidly. The group has drawn up a report, “Measures for Regulatory Reform and Competition Policy in the Telecommunications Sector,” which was released in November 2002.

The major points of the report are given below.

(1) Necessity of revising the system and basic viewpoints

- A. Technological innovation and the display of originality and ingenuity by enterprisers are promoted through further competition, leading to the development of a robust telecommunications market as part of the society’s infrastructure.
- B. In the telecommunications sector where technology rapidly changes, controls that are implemented before there is a demonstrated need for them are likely to become excessive or result in being inappropriate for the actual conditions. Therefore, controls should be applied *ex post facto* as a means of correcting problematic activities through the clear identification of prohibited acts in advance, rather than as a means of control placed in advance such as control relating to approval and permission.

(2) Ensuring consistency with the competition authority

With respect to regulations to ensure fair competition, the JFTC and government agencies in charge need to collaborate to make the rules for competition consistent between different sectors. This collaboration is needed to avoid the confusion caused by double standards and to ensure fairness and neutrality.

(3) The form regulations should take

- A. A regulation to relieve the congestion of facilities and equipment, such as a subscriber line network, is necessary as a transitional regulation to introduce some level of competition. However, government agencies in charge and the JFTC need to jointly verify the spread of competition in the market and review and revise the details of the regulations.
- B. The JFTC needs to be concerned with the objectives and details of regulations about so-called universal services from the viewpoint of their influence on competition.
- C. Controls other than the above that have been implemented in advance should be abolished, in the same way as controls for general goods and services. *Ex post facto* control that allows a wide margin of activity for businesses should be in place.

2. Strict Enforcement of the Antimonopoly Act

From a viewpoint of promoting competition in IT and the public service sectors, including the telecommunications sector, the JFTC established a task force for the IT and public service sectors

in April 2001. The purpose of the task force is to decide cases through the effective and quick gathering of information on cases relating to the violation and suspected violation of the Antimonopoly Act in these sectors.

The JFTC has dealt harshly with activities that may prevent fair competition in the telecommunications sector, and has recently taken the following measures. The above task force dealt with the case mentioned (3) below.

(1) Recommendation to Nippon Ido Tsushin Corporation

The JFTC found that Nippon Ido Tsushin Corporation compelled agents to sell cellular phones at the selling price designated by the corporation. The agents were engaged in the retail sales of cellular phones with the trademark of the corporation and directly or indirectly purchased them from the dealers or general dealers of the corporation in the Kanto area. The JFTC issued recommendation to Nippon Ido Tsushin Corporation in December 1999 to the effect that the above activity violates the provision of Section 19 of the Antimonopoly Act (Items 1 and 2 (restraint of resale price) of Article 12 of Designation of Unfair Trade Practices), and, therefore, Nippon Ido Tsushin should stop engaging in the practice.

(2) Warning to Nippon Telegraph and Telephone East Corporation

The JFTC suspected that Nippon Telegraph and Telephone East Corporation prevented DSL enterprisers, who wished to connect to a subscriber line network by entering into a mutual connection agreement, from taking up DSL services, thereby causing difficulty for the DSL enterprisers in carrying out their business activities, and placing the DSL enterprisers at a competitive disadvantage. The JFTC issued a warning to Nippon Telegraph and Telephone East Corporation in December 2000 to the effect that the above activity may violate the provision of Section 3 of the Antimonopoly Act, and, therefore, the corporation should refrain from engaging in the activity.

(3) Warning to Nippon Telegraph and Telephone East Corporation and Nippon Telegraph and Telephone West Corporation

The JFTC suspected that Nippon Telegraph and Telephone East Corporation and Nippon Telegraph and Telephone West Corporation charged a fee to users of rival enterprisers for engineering work. The JFTC believes this activity occurred while Nippon Telegraph and Telephone East Corporation and Nippon Telegraph and Telephone West Corporation carried out engineering work to replace safety equipment and upgraded the cables to metal cables for the users of these corporations free of charge when providing ADSL services. The JFTC issued a warning to both corporations in December 2001 to the effect that the activity may violates the provision of Section 3 of the Antimonopoly Act, and, therefore, the said corporations should refrain from engaging in the activity.

3. Amendment and publication of the “Guidelines for Promotion of Competition in the Telecommunications Business Field”

(1) Outline

Provisions concerning the promotion of free and fair competition among telecommunications companies were enacted as part of the Basic Law on the Formation of an Advanced Information and Telecommunications Network Society that was enforced in January 2001. Therefore, the

promotion of free and fair competition in the telecommunications sector has become one of the important policy problems for the government overall. Under these conditions, the JFTC drew up and published, together with the Ministry of Public Management, Home Affairs, Posts and Telecommunications, in November 2001 the “Guidelines for the Promotion of Competition in the Telecommunications Business Field.” These guidelines provide basic ideas regarding problematic activities in view of the Antimonopoly Act and the Telecommunications Business Law to promote free and fair competition in the telecommunications sector.

The above guidelines provide basic ideas regarding problematic activities in view of the Antimonopoly Act and the Telecommunications Business Law for each area of the following areas: (1)Section pertaining to interconnection and sharing of telecommunications facilities, (2)Section pertaining to the leasing of utility poles, ducts, conduits and other related facilities, (3)Section pertaining to the provision of telecommunications services, (4) Section pertaining to the provision of on-line content, and (5) Section pertaining to manufacture and sale of telecommunications facilities. The guidelines also state the specific measures to isolate information between a connection division and other divisions, the publication of the status of compliance with firewalls and the status of connection and collocation. It is hoped that these practices are carried out on a voluntary basis by the telecommunications carriers controlling the market.

(2) Amendment and publication of the guidelines

The number of cases that are subject to the above guidelines should be increased with changes in the competitive environment. The guidelines will also be flexibly reviewed and revised as appropriate, reflecting the results of the implementing the guidelines. In December 2002, the JFTC, working with the Ministry of Public Management, Home Affairs, Posts and Telecommunications, published an amendment of part of the above guidelines that included additions based on previous cases of applying the laws.

4. Future Approach

- (1) The JFTC has studied what a desirable competition policy should be for the development of the telecommunications sector, and has actively made proposals to and coordinated with the Ministry of Public Management, Home Affairs, Posts and Telecommunications, the ministry in charge of telecommunications, to make regulations and systems more competitive in the telecommunications sector.
- (2) The JFTC considers it important to work in collaboration with the Ministry of Public Management, Home Affairs, Posts and Telecommunications, and the Telecommunications Business Dispute-Settlement Commission, which has responsibility in this area, with the objective to promote free and fair competition in the telecommunications sector. The JFTC needs to collaborate closely with the Ministry of Public Management, Home Affairs, Posts and Telecommunications to draw up and enforce rules on the control placed in advance over connections. The JFTC also needs to develop measures for collaboration with the Telecommunications Business Dispute-Settlement Commission, for the smooth provision of information necessary for dispute settlement and the mutual exchange of opinions.
- (3) In addition, the JFTC will continue with the prompt and strict elimination of activities that violate the Antimonopoly Act to secure free and fair competition in the telecommunications sector. The JFTC will continue to review and revise, jointly with the Ministry of Public

Management, Home Affairs, Posts and Telecommunications, the existing Guidelines to meet the requirements of new systems.

3.5. MEXICO: FEDERAL COMPETITION COMMISSION

ADVOCACY ACTIVITIES OF FEDERAL COMPETITION COMMISSION IN THE TELECOMMUNICATIONS SECTOR

BACKGROUND

Telefonos de Mexico (Telmex) was privatized in 1990. The Ministry of Communications and Transport and the new owners agreed certain modifications to the Title of Concession (formerly granted in 1976) in order to allow Telmex to build, maintain, operate and exploit commercially a public telephony network by a term of 50 years.

The Modifications to the Title of Concession of Telmex refers to future legislation as being applicable, thus embracing the new statute. The Federal Law on Economic Competition (FLEC) came into force on the 22nd of June 1993 and the Federal Telecommunications Act came into force the 7th of June 1995.

Pursuant to article 63 of the Federal Telecommunications Act, the Ministry of Communications and Transport is empowered to establish specific obligations referring to the quality of service, information and rates to licensees of public telecommunications networks when they have substantial market power in the relevant market, according to the FLEC.

After privatization, although government granted to Telmex a six-year monopoly in long distance service, the government imposed several operation goals and regulatory provisions to Telmex:

- A 12% annual expansion of the number of telephones installed during the first years after privatization,
- A system to measure quality and reliability indicators, in order to monitor the performance of the services delivered by the company and,
- A program of social coverage, by establishing universal service obligations within a time frame for their implementation.
- A price cap regulation upon a basket of services¹
- Prohibition to incur in cross subsidization and monopolistic practices

BASIC LOCAL TELEPHONY

Although the basic local telephone services were formally open to competition before the privatization of Telmex, the investments needed to build local networks and the lack of a regulatory framework governing the interconnection among local networks discouraged competitors from entering to the market.

The publication of Local Service Rules in October 1997 and the development of new technologies made possible the entry of new competitors to local telephony.

¹ The basket of services included installation, rental charges, local services and long distance services, both domestic and international.

The FCC participated closely with the Ministry of Communications and Transport, in the definition of the rules for the opening of the market.

LONG DISTANCE MARKET

Telmex was the only supplier of long distance services until August 1996 when new companies entered to the market, although in this first step of the opening up the new long distance operators only could offer unswitched long-distance service. Since January 1997 when the supply of interconnection became effective the new operators can offer also switched long distance services.

Resolution of the FCC which declared Telmex as agent with substantial power in five relevant markets

In 1997 Telmex was declared agent with market power in five relevant markets by the FCC: local telephony, local access, national and international long distance, and interurban transport. The possibility to declare dominance was established in the Telecommunications Act in order to empower the Federal Telecommunications Commission to impose specific regulations upon the dominant firm.

Basic local telephony. - The basic local telephony leads traffic among users of the same central or users of the same group of local service centrals that does not require dialing an access prefix, irrespective of whether this traffic is originated or terminated in a wire or wireless public network, and the rate collected is independent of the distance. The market share of Telmex in this market was around 99%.

Access. - The service for access to end users provides physical and logical connection that makes it possible to transmit traffic between a public telecommunications network and a local network, which provides the service known as "last mile", the connection from the local telephone network to each user. The market share of Telmex in this market was around 99%.

National long distance service. - The national long distance service leads traffic among centrals that are not in the same group of local service and requires dialing an access prefix. The market share of Telmex in the national long distance service was approximately of 78%.

International long distance. - International long distance services cover the initiation and termination of international calls in Mexico. These calls are originated by dialing a protocol of calling that includes a specific prefix of an area where the call is ended. The market share of Telmex in the international long distance service was approximately of 65%.

Inter-urban transportation. - The inter-urban transport service consists of routing traffic between two or more long distance networks. This service is required from Telmex by other operators to transmit long-distance communications to the cities that are not open to pre-subscription, and to areas in which long distance operators do not have their own infrastructure, as well as to overflow, which happens when the transmission of an operator becomes saturated and the traffic "overflows" toward circuits of other operators. The market share of Telmex in the market of inter-urban transportation was around 98%.

Telmex filed several appeals before the FCC and amparos² that delayed the enforcement by the Federal Communications Commission of a Dominant Carrier declaration. The claims filed by Telmex are based on the unconstitutionality of the Telecommunications Act, and the lack of jurisdiction of the FCC for issuing the declaration of Telmex being an agent with substantial power in the five markets.

Resolution of the Federal Telecommunications Commission (Cofetel) establishing specific obligations to Telmex in its character of dominant operator in five relevant markets of services of telecommunications

On 11 September 2000, Cofetel issued a resolution establishing specific obligations to Telmex related to rates, quality and information, in its character of licensee of a public network of telecommunications with substantial market power in five relevant markets.

The resolution of Cofetel ended the administrative proceeding initiated the 27th March of 2000 pursuant the Federal Law of Administrative Procedure initiated the 27th March 2000 to establish specific obligations to Telmex according to Article 63 of Federal Telecommunications Act.

The resolution establishes for Telmex rate criteria based on costs, in order to avoid squeezing. Also, the resolution requires that the average weighed rate of long distance, as well as the other services opened up the competition, allows to recover the average cost of providing the service, including the capital cost.

The resolution establishes that rates set by Telmex for “essential services”, as provision of ports, co-location, local transit, invoicing and collection, emergency services, services of operators, installation and renting of connections of long distance, will have to recover the cost of providing these services.

On the other hand, the resolution of Cofetel decrees that the local service rates set by Telmex will remain unchanged in the whole country until January 2003. In addition the rates of the other services included in the basket of controlled basic services can only be changed taking into account volume, distance and schedule.

As regards quality of the services, Telmex was bound to build and release quality indexes for the services supplied to consumers and other licensees of public networks of telecommunications. In addition, Telmex is obligated to follow a principle of “first come, first served” for attending the requests of other licensees as well as its own subsidiary companies.

Finally, the quality of services supplied by Telmex to other licensees must have the same level as those provided to its subsidiary in the long distance market, LADA, moreover Telmex will have to allow that the LD operators share ports and interconnection links.

With respect to information, Telmex will have to establish a technical database that facilitates the interoperability of networks of telecommunications, as well as allow the access by other licensees to this information. Also, Telmex will have to disclose the indexes of quality of the service to users and other licensees of public networks of telecommunications. In order to avoid cross subsidization, Telmex will have to disclose the information of separated accounting by service.

² *Amparo* lawsuit is a legal action of last resort brought by an aggrieved party before a District Court or Supreme Court of Mexico seeking reparation for, or the suspension or annulment of an act by a government authority that violates the complainant's constitutional rights.

3.6. NETHERLANDS COMPETITION AUTHORITY

Information on Advocacy in the ICT-sector

Under the present system the Ministry of Economic Affairs regularly asks the Director General of the Netherlands Competition Authority (NMa) for advice in the process of drawing up legislation or decisions in which aspects of competition law play a role. In addition, the NMa gives advice informally, in most cases on request of Ministries.

The present Competition Act does not contain provisions that explicitly extend to the Director General the power to give advice. Equally, the absence of the prerogative to give advice cannot be derived from the Act. In one specific Act, the NMa is explicitly granted advisory powers.

Section 18.3 of the Telecommunications Act [*Telecommunicatiewet*] stipulates that the Minister of Economic Affairs¹ must grant the Director-General of the NMa the opportunity to give advice on the effects, in terms of competition law, of draft decisions to refuse or revoke a licence.

The Minister has, in fact, presented a number of important matters to the Director General of the NMa for advice, pursuant to the Telecommunications Act. Advice was requested with regard to the aspects relating to competition law of plans, on the basis of which licences were to be allocated. The Director General of the NMa was asked to give advice on the following matters, with reference to the Telecommunications Act: UMTS, Zero Base², Terrestrial Trunked Radio³, Digital Video Broadcasting Terrestrial⁴, Wireless Local Loop, DCS-1800.⁵ All the fore-mentioned advice of the Director General of the NMa is connected with the question whether the allocation of a licence will lead to the creation or strengthening of a dominant position on the relevant market.

In theory, the Director General of the NMa only has a right to advise. However, practice showed that policy makers in these cases do not easily deviate from (non-binding) advice.

In addition to giving advice in accordance with the above-mentioned (legal) powers, a practice of giving advice on an *ad hoc* basis has developed, which does not have a statutory basis.

The NMa has, for instance, given advice on an informal basis on the implementation of the new EU-directives concerning the revised ONP-rules. The NMa has also given advice to the Ministry of Transport, Public Works and Water Management on a draft Act which should enable internet service providers to get access to cable networks in order to provide internet services.⁶

In the end, however, it is the legislator that decides based on all policy aspects concerned.

¹ Until recently this was the Minister of Transport, Public Works and Water Management. Since the policy regarding Telecommunications and Post has been brought under the responsibility of the Minister of Economic Affairs, it is the Minister of Economic Affairs that is advised on these matters by the NMa.

² In this case, a distribution proposal of FM radio frequencies was presented to the Director-General of the NMa for advice.

³ In this case, the proposed issuing of two licences for a digital telecommunications system was presented to the NMa.

⁴ In this case, the NMa advised the Ministry of Transport, Public Works and Water Management to exclude cable companies from a licence, since they were dominant players in the market for the transmission of TV-signals (an exception was made for cable companies who would have a minority share in a consortium).

⁵ All the recommendations and protocols referred to as examples in this letter can be found, in Dutch, on the NMa's website (www.nmanet.nl).

⁶ Now this area of policy falls under the responsibility of the Ministry of Economic Affairs.

Another example of advocacy of the NMa without an explicit statutory basis is the (public) discussion that is going on concerning a chosen government policy regarding submission fees in the Dutch cable sector. This discussion concerns the roll out of a second competitive infrastructure, i.c. a fully digital cable network to the end-user. The danger exists that the expenses of this digitalisation will be passed on to the television viewer, who is a captive customer.

This discussion is still going on. We perceive that the Ministry of Economic Affairs considerably appreciates our contributions regarding this subject. It also contributes to the understanding of competition implications of possible policy making of the Ministry.

3.7. ROMANIA: COMPETITION COUNCIL

COMPETITION ADVOCACY IN TELECOMMUNICATIONS

	<i>Sectoral Regulator/Competition authority</i>	<i>Role and methods of cooperation</i>	<i>Industry background</i>	<i>Competitive objectives and advocacy methods</i>	<i>Source of authority to engage in advocacy</i>	<i>Efforts over time</i>	<i>Efficiency</i>
Armenia	State Commission on Protection of Economic Competition					Cases of competition legislation enforcement: tying.	
France	Telecommunications Regulatory Authority (ART) / Competition Council (CC); General Directorate for Competition, Consumer Affairs and Fraud Control (DGCCRF).	ART: allocate frequencies and numbers; approve incumbent interconnection tariffs; settle disputes. ART has to refer to CC any abuse of dominant position or any anti-competitive practice in the sector. ART and CC may seek reciprocal advice from each other.	The sector has been considerably transformed over the last five years from a monopolistic market structure (fixed telephony) to a multiform and competitive sector (fixed telephony, mobile telephony, internet access).	Ensure an effective and fair competition among network operators and telecommunications service providers, in the interest of the users. CC can be asked to provide its opinion on competition by the Government, parliamentary committees, local authorities, professional organizations, trade unions or consumers.	Telecommunications Act 1996.	Newcomers entered the market easier due to regulator's and Competition Council's decisions entailing asymmetrical regulation on the incumbent. As an interim measure, CC stopped France Telecom's subsidiary Wanadoo to market a new product until all ISPs had sufficient information, in order to eliminate any distortion of	Increased competition and lower prices in long distance and mobile markets. Transparent billing information in mobile. France Telecom forced to give access to ISPs to its network on a cost-oriented

				Publication of decisions (with access via the Internet). Cases presented in the press or other media. Rating of mobile operators as an incentive to competition.		competition.	base and let other competitors order quickly and freely ADSL access thanks to an Extranet server.
Ireland	Commission for Communications Regulations (ComReg) / Irish Competition Authority (an advocacy division inside)	Formal (cooperation agreement, December 2002): - exchange of informations; - consultation; - avoid duplication in performing similar functions.	Fully liberalised in December 1998. Incumbent monopolist operator was privatised in 1999 (Eircom). It was obliged by the Government to sell its stake in the Dublin's local monopoly cable TV and, in 2001, it sold its mobile telephony company. <i>Markets:</i> 1/ Voice telephony – 86 licensed operators (new	Analyse any practice that might affect competition; carry out investigations; advise the Government on the implications on competition of proposals for legislation; publish notices containing guidance on how legal provisions may be complied with;	Competition Act 2002	ComReg is to relax rules for wireless operators in an attempt to spur competition. It will issue new-style licences in order to provide a more stable framework. <i>Cases:</i> Abuse of dominance from the national state owned monopoly railway company which refused to negotiate for the use of its cable network with	The critical role of the national regulator, as competition law enforcement is time-consuming and expensive.

	Minister for Marine, Communications and Natural Resources	Power to issue policy directives (in the near future, a policy directive to ComReg to order telecoms firms to offer flat-rate internet access services.	entrants – 21% of the market of fixed line). 2/ Mobile – two major players (54% and 40% of the market, respectively). 3/ Data traffic and Internet access – internet penetration – 51% 4/ Local loop unbundling – very slow, the highest monthly rental price for unbundling in Europe and an above average price for connection.	complied with; identify and comment on constraints on competition imposed by administrative practice; inform public about issues on competition. promotion of competition.	Communications Act 2002	other telecoms operators. Access to the local loop. Duration of mobile contracts. Subsidies by a mobile operator for its own sales arms detrimental to independent agents. Dominance and joint dominance.	
Japan	Ministry of Public Management, Home Affairs, Posts and			Promotion of free and fair competition among	Telecommunications Business Law	JFTC has been involved in the study group that has	

	Telecommunication; Telecommunications Business Dispute Settlement Commission//Japan Fair Trade Commission (JFTC)			telecommunications companies.	Antimonopoly Act	drawn the report “Measures for Regulatory Reform and Competition Policy in the Telecommunications Sector” (nov. 2002). Main conclusions: - necessity to revise the system (for instance, to switch to <i>ex- post</i> controls to correct from <i>ex- ante</i> controls, like approvals, permissions, etc. - ensure consistency with the competition authority (avoid confusion created by double standards). JFTC (together with the Ministry of Public Management, Home Affairs, Posts, and Telecommunications published “Guidelines for the	
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						Promotion of Competition in the Telecommunications Business Field” JFTC established a task force for IT and public services (2001). Antimonopoly Act enforcement – cases: - resale price maintenance; - price discrimination.	
Mexico	Federal Telecommunications Commission (Cofetel)/Federal Competition Commission (FCC)	Cooperation in the definition of the rules for the opening of the market.	Telefonos de Mexico (Telmex) was privatised in 1990. It has 99% of basic local telephony, 78% in national long-distance service, and 65% in international calls.		Federal Law on Economic Competition (1993) Federal Telecommunications Act (1996)	Cofetel issued a resolution establishing specific obligations to Telmex related to rates, quality and information, due to its substantial market power in five markets.	
Netherlands	Netherlands Competition Authority (NMa)			NMa regularly gives advice at the request of the Minister of Economic Affairs and to other ministries in the process of drafting	There are no provisions in the Competition Act to empower NMa to give advice.		

				legislation involving competition law issues.	However, the Telecommunications Act provides that the Minister of Economic Affairs must grant the Director General of NMa the opportunity to give non-binding advice on the possibility to create or strengthen a dominant position when approving a licence.		
Romania	The National Regulatory Authority for Communications (NRAC - 2002)/Competition Council (CC - 1996)	NRAC acts as a regulatory authority in accordance with European Union directives, as an arbitrator and ruling authority in the resolution of disputes between operators, in order to ensure free competition and protect consumer interests. CC enforces general competition protection legislation (including to telecommunications sector).	Fixed telephony and leased lines markets have been liberalized starting January 2003. Activities may now be undertaken under the conditions of the general authorization regime; individual licences are only required for the use of radioelectric frequencies and numbering resources. Any company intending to provide communications networks or services must send to NRAC written notification of its intention at	When NRAC intends to adopt supplementary regulations which could have a significant impact on the relevant market, it must first launch a consultation procedure. Thus, NRAC must publish the text of the proposed measures on its website and interested parties have a certain period in which to submit their written comments.	Competition Law Law on the general legal framework on communications Government Ordinance on access and interconnection	Papers and speeches by officials of the CC, advocating for a competitive environment, general authorization system and evaluating the impact of market liberalization. CC – in cooperation with NRAC – adopted Guidelines on the enforcement of competition protection rules to access agreements in electronic communications markets.	The regulatory framework for a competitive environment is in place, but results are to be seen in the near future. Competitive pressures from the mobiles market determined the incumbent operator of the fixed network to

		The Communications Ordinance states that where the regulations in force ask that certain obligations be imposed, modified or withdrawn as a result of market analyses, NRAC must determine whether effective competition exists on the relevant market, based on certain regulatory criteria drawn up by NRAC in collaboration with CC. The Ministry retains certain regulatory powers, among which power to draft policies and strategies of the sector.	of its intention at least seven days prior to commencing activities. Incumbents are required to provide interconnection with new entrants. Other markets were already competitive. An operator is considered to have significant market power in a certain market if, individually or together with other operators, it enjoys a position equivalent to a dominant position.			NRAC – together with CC – adopted Guidelines on identifying relevant markets, market analysis and the determination of significant market power. Competition law enforcement: - case on an agreement involving the incumbent operator and including provisions of non-competition on a certain market; the case was finalized with the highest fine ever imposed by the CC. - case on an agreement between three existing mobile operators aimed to determine a	network to decrease tariffs of long distance calls.
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	Ministry of Communications and Information Technology					fourth one to sign interconnection agreements.	
Slovakia	Telecommunication Office (TO) / Antimonopoly Office (AMO)	Due to previous insufficient cooperation, a formal agreement providing for coordination and exchange of information has been signed by TO and AMO.	Slovak Telecom (ST) has been privatised in July 2000. The market has been liberalised starting January 1 st 2003. Liberalization did not yet produce any effects.	Active involvement of AMO in drafting governmental policies and regulations (including the new law on electronic communications).	Act on Protection of Competition.	Analysis of complaints from ISPs against ST. President of AMO participates in Government meetings. AMO publishes on its website press releases and opinions on various issues in telecoms. AMO advocates for the independence of TO.	Liberalization so far exists only on the paper. TO has done little to support the creation of a competitive environment, like for instance its lack of reaction in solving disputes between alternative carriers and the incumbent ST.
United States	The Antitrust Division of the Justice Department (AD)	Direct responsibility for overseeing competitive issues in telecoms markets. Limited jurisdiction	1982 Modified Final Judgment (MFJ) of the antitrust case US vs. AT&T largely determined the shape of the US telecommunications	AD advocates pro-competitive principles mainly in formal filings before the FCC, as well as in less formal contacts and	Telecommunications Act (1996). Bell companies were allowed to re-enter the long-distance market within their local regions, but	AD extensive comments with the FCC as it promulgated implementing regulations; the Department made	Increased competition and reduced prices in long distance and mobile markets.

	Federal Trade Commission (FTC) Federal Communications Commission (FCC) State attorneys general and state regulatory commissions	over certain telecommunications companies, but also handles certain types of civil cases in these markets. Authority to review telecommunications mergers under its “public interest” standard and has generally regulatory authority over the industry. Can also become involved in competitive issues in telecommunications.	markets, by broking up the Bell System and precluding the separated regional companies with their local monopolies from entering the long distance markets. In 1996, the MFJ was superseded by the Telecommunications Act, which sought to promote broader competition in the industry. <i>Long-distance telecommunications market</i> – competitive, no carrier has been considered dominant since 1995. <i>Local telecommunications market</i> – the four regional Bell companies continue to own the vast majority of the nation’s local exchange lines, but	speeches to federal and state regulators and intersted parties. AD also undertakes traditional antitrust enforcement activities in telecommunications.	with the condition of taking measures to open their local markets. DoJ evaluations of Bell company applications have to be given “substantial weight” by the FCC.	recommendations regarding the unbundling and pricing of telecommunications network elements AD advocated for the local telephone market to be “fully and irreversible open to competition”. AD monitoring of the markets <i>in anticipation</i> of applications from the companies to ensure that evaluations of those applications are complete. From 1996 through 2002, AD evaluated 31 Bell applications covering 36 states. AD involvement in the MVPD market – more traditional antitrust investigations and <u>litigation, mainly in</u>	markets. Mixed results in the local telephony market.
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			the FCC data continue to show the development of competition in this market. <i>Mobile telecommunications market</i> – at the end of 2000, 90% of the US population had access to at least three mobile operators, while 75% had access to at least five operators. <i>Data and Internet telecommunications services</i> – competitive and unregulated. One company is dominant in narrowband Internet services with 50% of the subscribers. <i>Multichannel Video Programming Distribution (MVPD)</i> – there is competition between landline cable television providers and direct broadcast			order to block mergers with anticompetitive effects.	
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			satellite service providers.				
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3.8. ANTIMONOPOLY OFFICE OF THE SLOVAK REPUBLIC

COMPETITION ADVOCACY IN TELECOMMUNICATION SECTOR

The Antimonopoly Office of the Slovak Republic (hereinafter AMO) is a central state administrative body responsible mainly for protection of the economic competition, and creation of conditions for its further development.

In addition to sanctioning anti-competitive practices (such as an abuse of a dominant position on the market, cartel agreements...) and monitoring market structures by means of concentration assessment, the duty of the AMO is also to monitor and call for compliance and proper application of competition principles in the process of forming policies and legal framework of our community and to provide **competition advocacy**.

In the recent time the AMO has actively been involved in drafting governmental and economy policies and through its comments the AMO proposed a number of alternative solutions resulting to promotion of competition particularly in the telecommunication sector.

The telecommunication sector is represented in particular by incumbent operator Slovenské telekomunikácie, a. s. (hereinafter Slovak Telecom) which provides national and international telephone services, and a wide portfolio of data services. The Company also provides distribution and transmission of radio and television signals and offers a wide range of value added services. In July 2000, the German company Deutsche Telecom AG became the strategic partner for Slovak Telecom with 51% of shares. The State owns (through the Ministry of Transport, Posts and Telecommunication) 34% of shares of Slovak Telecom and 15% of shares are owned by the National Property Fund.

The main reason for focusing competition advocacy on the telecommunication sector has been an increasing number of complaints lodged by Internet Service Providers towards incumbent operator Slovak Telecom.

In the course of liberalization process the telecommunication sector has gone through radical change from a monopoly network industry towards a modern dynamic sector with enhancing amount of various operators. In spite of this the incumbent operator or entrepreneurs that might enjoy a dominant position on relevant market have been faced with temptation to abuse of such a position. AMO realized that its activities would have to be highlighted on competition advocacy along with the enforcement of competition law particularly in the telecommunication sector.

First and foremost a practical realization of the AMO's intention to intensify competition advocacy was aimed to uphold the effort in eliminating an adverse development in the area of abuse of dominant position by Slovak Telecom and diminishing a number of misunderstandings and discrepancies with the Telecommunication Office of the Slovak Republic regarding specification of particular competencies in the investigation process.

Due to insufficient cooperation between the AMO and the Telecommunication Office, the AMO initiated signing an agreement that formulated an intention to cooperate in the matters of common interest, respecting the rights and obligations which arising for both bodies from legal rules with the aim to assign:

- co-ordinated performance of matter-of-fact responsibilities of AMO and the Telecommunication Office in the interest to prevent the creation of positive or negative competence conflicts, particularly prevent to issue decisions which collide to each other,
- same interpretation of terms used in acts and in other generally obligatory legal rules relating to the competition and telecommunication area,
- cooperation for determination of consistent procedures solving the cases in the telecommunication area,
- informing each other about facts relating to abuse of a dominant position, inspection over the entrepreneurs with dominant position in the relevant market in the telecommunication area pursuant to Act on Protection of Competition or in the telecommunication market pursuant to the Act on Telecommunication and Regulation in the telecommunication area.

The AMO and the Telecommunication Office agreed that it was in their interest to inform each other about all relevant facts relating to their activity. Both institutions should provide each other with information given by the entrepreneurs in connection with their activities and proceedings if this information is necessary for fulfilling their tasks and if reasonable legal objections against such exchange of information do not exist.

The AMO and the Telecommunication Office should regularly inform each other about conduct of entrepreneurs acting in the telecommunication area which might have the nature of abuse of a dominant position pursuant to the Act on Protection of Competition or about conduct of the entrepreneur with significant influence on the telecommunication market pursuant to the Act on Telecommunication which is in contrary to the Act on Telecommunication.

Moreover both Authorities should inform each other about matters relating to the telecommunication area, which have been subject to discussion with representatives of European Commission, including information about facts relating to responsibility of the Telecommunication Office in relation to responsibility of the AMO.

Based on the abovementioned agreement and by reason of magnifying portion of cases concerning abuse of a dominant position in the telecommunication sector the AMO asked the Telecommunication Office for better enforcement of common basic competitive objective, which was an introducing equal and transparent conditions for the development of the telecommunication market so that its users would be provided with good quality of telecommunication services at affordable prices and - at the same time - conditions would be established for joining the European Union and global structures.

In the connection of described circumstances the AMO decided to publish in addition to valid decisions also declarations and standpoints about situation in the telecommunication sector on its internet website and in other mass-communications. For instance:

Last year the AMO issued preliminary ruling by which it obliged the Slovak Telecom to refrain from providing telecommunication services based on ADSL. To make some explanation the AMO was issuing the statement on its website and in a couple of newspapers. AMO clarified that starting the commercial pilot ADSL by the Slovak Telecom has affected the entry of this entrepreneur to the new market of providing telecommunication services of the high-speed data transmission. Conditions to entry the market, determined by the Slovak Telecom, could affect

situation and development of competition in market of providing telecommunication services of the high-speed data transmission, where the relatively high dynamics of development of competition is assumed, regarding the intensive interest of many companies to entry this market. Worries of possible negative influence on entrepreneurial surroundings in this newly created market with a possible deformation of its structure has particularly arisen from conditions determined by the Slovak Telecom, which have appeared to be quite disadvantageous for competitors and on the other hand quite advantageous for Slovak Telecom itself. It was necessary to prevent from negative development in this market by issuing preliminary ruling, which froze providing of this service for certain period under conditions such given.

Afterward on the basic of the AMO activities ADSL project started its operation on the basic of non-discriminatory conditions.

At the same time the public and media were thoroughly watching the conditions of providing the service of Internet connection through the number 019XY, determined by the Slovak Telecom. The AMO issued another declaration in which encouraged customers to make a complaint on discriminatory behavior of Slovak Telecom to the Telecommunication Office as the state administration body empowered to act in the matter of regulation and control of telecommunication service providers and operators of telecommunication networks.

Moreover the AMO focused its endeavor to improve competition advocacy on other central state administrative body – Ministry of Transport, Posts and Telecommunication (hereinafter Ministry of Telecommunication). This Ministry represents the major legislator in the telecommunication sector. The AMO decided to participate to full extent in the process of preparation of legislative framework for telecommunication sector mainly in drafting the new law on electronical communications. This new law should cancel and replace present telecommunication law and will be adjusted to newly modified conditions on the market of product and services. It will also create legal framework with regard to position of an independent regulatory body for sector, provision of universal telecommunication services and creation of standard licensing system by means of promoting transparency, competition and simplifying regulatory environment.

The AMO nominated its own experts to the working group for preparation of the new law, which was created by the Ministry of Telecommunication. In this group representatives of the AMO enforced imbedding competition principles resulting to new regulatory framework which would boost development of competition, better price for consumers, good quality of services, better choice and at the same time transparency for all players on telecommunication markets.

The next goal of the AMO is to enforce via advocacy the most significant long-term strategic role in the telecommunication area, which are the liberalization of the telecommunication market and support of free competition. To be able to comply with those basic requirements, it is necessary to fully liberalize the telecommunication market and separate the execution of ownership rights in the joint-stock company Slovak Telecom with the ownership share of the state from regulatory activities, which is also required by the EU. This goal could be explained and forced in particular by the Chairwoman of the AMO who regularly takes part in discussions of the Government of the Slovak Republic or through advocating as an official member of the Council of Economics Ministers and a member of the Economic Council of the Government of the Slovak Republic. Thus, the AMO is directly engaged in individual government policies and has the opportunity to express itself from the viewpoint of protection of competition.

The AMO exerts a huge effort to advocate for separation of the Telecommunication Office's budget from the budget of the Ministry of Telecommunication and creation of its own budget chapter. Separated financing system of the regulatory body needs to be realized till the accession of SR to EU at the latest, as it is one of the EC requirements to have the Telecommunication Office financed independently from Ministry. Later - depending on the economic situation in the state - it may be co-funded from the fees for regulatory performance.

The telecommunication market in Slovakia has *de jure* been liberalized. The Slovak Telecom had exclusive rights to provide basic public telephone service guaranteed by 31 December 2002 within the meaning of the Telecommunication Act. According to the Act, as from 1 January 2003, also other telecommunication operators would be allowed to start provision of the public telephone service through fixed networks. From that date, users of the public telephone service should be enabled to choose a telecommunication company for long distance and international traffic through pre-selection of the number or on call-by-call basis by dialing a prefix.

Despite a requirement of the AMO to ensure the opening of telecommunication market at the beginning of the year, the Telecommunication Office has done little to support free competition. Unfortunately although the monopoly enjoyed by Slovak Telecom expired at the end of 2002, the AMO promulgated during the meeting of both offices' representatives that market liberalization so far exists only on the paper. Moreover according to statement of alternative providers failure to use even those authorities that the Telecommunication Office has under valid legislation, and its deep lack of activity have seriously hindered the development of the telecommunication market.

The AMO also declared its dissatisfaction with the means by which Telecommunication Office implemented the telecommunication law in practice, especially the responsibility to create conditions for fair, transparent, and competitive space in the telecom market. The AMO expressed an opinion that alternate carriers have been unable to establish operations, even after receiving fixed-line licenses, because they have not reached agreement with Slovak Telecom on the use of the operator's local loops - the final connections with end users.

Along with the AMO, Ministry of Telecommunication has also criticized the Telecommunication Office, saying that the regulator had failed to complete certain tasks, including establishing a legal definition for a "carrier with significant influence" - a key factor in implementing regulatory mechanisms. Telecom Minister has stressed the need to establish increased independence for the regulator, which up to now has been funded by Ministry of Telecommunication. He has also proposed transferring the state's minority stake in Slovak Telecom to a different institution to ensure regulatory independence on the suggestions of the AMO and he also added that the law on electronic communications expected this year should smooth out whatever wrinkles remaining in the liberalization of the country's telecom market.

The AMO hopes that the proposed new law will also increase the competence of the Telecommunication Office that has struggled with a lack of manpower and budgetary independence, as well as with the inability to enforce its decisions.

The next form of advocacy taken by the AMO was presentation of the AMO's expert at the international conference on telecommunication sector held in Bratislava in January 2003. At the conference the AMO explained the approach and investigative procedure regarding abuse of a

dominant position in telecommunication sector, clarified the relationships between the AMO and the Telecommunication Office and declared an opinion that Slovakia would carry out the following steps:

- The regulatory authority must define the telecommunication operators with a right and obligation of interconnection
- The regulatory authority must provide for the compliance the basic principles of the telecommunication networks interconnection and the calculation of the interconnection charges of operators with a significant market power introduced in the Directive 97/33/EC and the Recommendation 98/195/EC;
- The regulatory authority must provide for publishing a referential quotation of network interconnection of operators with a significant market power including their interconnection prices.

The AMO uses many other possibilities to increase advocacy in telecommunication sector; it provides in the newspapers and other mass-communications media the full statements and declarations and a lot of other information on its activities in this area. Twice a month the AMO publishes information on initiated administrative proceedings, on issued decisions, on appeals submitted against decisions of the AMO and some other information including activities in telecommunication sector in daily newspaper. Purpose of this activity is to inform entrepreneurs on proceedings initiated in the AMO and thus allow them to express or introduce possible objections to the administrative proceedings, primarily in an area of concentrations.

The AMO is obliged to publish valid decisions, notifications of concentrations, warnings directed to the state administrative authorities and municipalities, if they restrict competition in some way and information on initiated proceedings in all other matters coming out from the Act on Protection of Competition . It is applied also for the telecommunication sector and the AMO fulfils this obligation by publishing the mentioned information on the website and by other means.

The Act on Free Access to Information is in force from January 1, 2001. Pursuant to this Act is each natural and legal person allowed to get information, which the relevant state authority has at its disposal. This possibility has been used really actively; in the course of recent years there were about 80 requests from entrepreneurs from telecommunication area.

3.9. UNITED STATES DEPARTMENT OF JUSTICE

SUBMISSION ON TELECOMMUNICATIONS TO THE ICN COMPETITION ADVOCACY SUBGROUP

Several federal and state regulatory agencies have responsibilities for matters that impact competition in United States telecommunications markets. The Antitrust Division of the Justice Department has the most extensive, direct responsibility for overseeing competitive issues in these markets since it is the only federal competition agency with full jurisdiction over common carriers. The Division primarily enforces the Clayton Act and the Sherman Act by reviewing proposed mergers and existing corporations' competitive conduct. The Division also participates where appropriate in proceedings of other agencies which require consideration of antitrust laws or competition policy. The Federal Trade Commission (« FTC ») has limited jurisdiction over certain telecommunications companies, but also handles certain types of civil cases in telecom markets. The Federal Communications Commission (« FCC ») has authority to review telecommunications mergers under its « public interest » standard, which can include competitive considerations, whenever a common carrier or radio license transfer is involved, and has general regulatory authority over the industry. State attorneys general and state regulatory commissions can also become involved in competitive issues in telecommunications markets.

This paper focusses on the work of the Department of Justice's Antitrust Division in advocating and enforcing competition in various telecommunications markets. The Division's work in these markets involves both antitrust investigation and prosecution as well as regulatory advocacy. The Division seeks to enforce the antitrust laws passed by the Congress, which are designed to protect consumers, not competitors, from anticompetitive combinations and conduct. The Division also advocates pro-competitive principles in formal filings before the FCC as well as in less formal contacts and speeches to federal and state regulators and interested parties.

The sources of authority for the Division to engage in antitrust advocacy related to telecom markets are discussed below, followed by a description of the various telecommunications markets in which the Division has been involved. Lastly, two distinct examples of Division advocacy are presented: local telephony and multichannel video programming distribution (« MVPD »). Since 1996, and the passage of the Telecommunications Act, the Division's efforts to encourage the development of competition in the local telephone market have focused primarily on advocacy efforts before the Federal Communications Commission (« FCC »). During this same time frame, the Division has pursued several investigations related to MVPD which resulted in the filing of formal complaints in the United States District Courts and the abandonment of the proposed, problematic transactions by the defendant-parties.

1. The Telecommunications Act of 1996

The United States telecommunications markets have been in large part shaped by the United States v. AT&T antitrust case and 1982 consent decree, the Modified Final Judgment (« MFJ »), that broke up the Bell System and precluded the separated regional companies with their local service monopolies from entering the long distance markets. For 14 years, the Division had a special role in overseeing large parts of the telecom industry under this decree, in addition to its traditional antitrust enforcement responsibilities.

In 1996, the MFJ was superseded by Congress's passage of the Telecommunications Act, which sought to promote broader competition in the telecommunications industry. The Act includes provisions that were designed to promote the development of local competition by requiring the regional Bell companies to provide certain facilities to new entrants, including interconnection to the incumbent network, unbundled network elements (« UNEs, » such as local loops) which can be combined with each other or with the entrant's own facilities to provide local service to end-user customers, and total service resale of local service. Via oral and written testimony from the Assistant Attorney General in charge of Antitrust, the Department advocated to Congress what provisions should be included in the Telecommunications Act, regarding both the substantive local-market-opening measures required of the Bells as well as the Department's role under the proposed legislation.¹ Section 271 of the Act sets forth the conditions under which the Bell companies can re-enter the long distance market in their local service regions. The Bells are required to show that they have satisfied a 14-point checklist for opening their local markets to competition, as well as establishing a separate subsidiary for long distance activities for at least three years and demonstrating that their entry is in the public interest, before they can begin providing in-region long distance. Section 271 must be satisfied on a state-by-state basis. The FCC has responsibility for determining whether Section 271 has been satisfied for any state, but the Department of Justice has a special role in the 271 process. According to 47 U.S.C. ' 271 (d)(2)(A), the Commission must notify the Department of any 271 application, consult with the Department about the application, and include any Department comments in the Commission's public record of its decision. Department of Justice evaluations of Bell company applications must be given « substantial weight » by the FCC. The FCC is not required to give this same deference to the comments of any other party to the proceeding.

2. Telecommunications Markets in the United States

1. Long Distance Telecommunications Services

The MFJ which settled the United States vs. AT&T antitrust case broke up the AT&T/Bell system and precluded the separated regional companies with their local service monopolies from entering the long distance markets. Before the decree, AT&T had more than 90 percent of the market for long distance services, but since the decree, competition has become extensive in the U.S. No carrier has been considered dominant since 1995. The three leading long distance carriers are AT&T, Worldcom and Sprint, which combine for approximately 60 percent of the market. Average prices have remained relatively stable for the past few years at approximately 11 cents per minute. Discounted plans have made minutes available for as little as 5 cents per minute, but recent indications suggest that carriers may be raising the prices and costs for discounted plans. As noted above, the Telecommunications Act of 1996 altered the competitive landscape for both long distance and local services. As of December 31, 2002, Bell companies

¹ Congressional testimony and statements of former Assistant Attorney General Anne Bingaman are available at www.usdoj.gov/atr/public/testimony/testimon.htm. At the same time the department was advocating before Congress, a motion filed by the Department pursuant to the MFJ was pending with the District Court; this proposal, if adopted by the court, would have permitted a limited trial of in-region long distance entry by a Bell company once that company had taken certain local-market-opening steps, very similar to those eventually contained within the Act. Once the Act was passed by Congress, it superseded the MFJ and the Department's pending Customers First motion.

have gained approval to offer long distance services within their local regions in 35 states and have quickly gained market share in those states. It is still uncertain whether the additional entry by the Bell companies will bring prices down further.

2. Local Telecommunications Services

The four regional Bell companies, Verizon, SBC, BellSouth, and Qwest, continue to own the vast majority of the nation's local exchange lines in their separate geographic regions. The Telecommunications Act of 1996 has had mixed success thus far introducing competition into this market segment. Overall, competitors serve nearly 12 percent of the nation's 189 million total switched access lines. In particular states, competitive shares are as high as 20 percent or more. The continuing economic downturn, reflecting in part the prior overvaluation of stocks and the past year's revelations of accounting problems, has taken a toll on competitive telecommunications companies: competitor market capitalization has fallen from its 1999 high of \$86 billion, to \$32 billion in 2000, to \$4 billion in 2001. The number of facilities-based competitive local exchange carriers (« CLECs ») has dropped from some 300 in 1999 to about 70 in 2002. Nonetheless, the FCC data continue to show the development of competition in the local telephone market: competitor growth, measured in lines served, continues although at a somewhat slower pace -- 10 percent growth in the most recent six months as compared to 14 percent growth in the previous six months.² Throughout the process, prices have remained roughly constant. The Division remains hopeful that sustainable local competition will continue to develop as a result of the Telecommunications Act.

3. Mobile Telecommunications Services

Competition in mobile telecommunications services has improved dramatically in the U.S. in the past ten years with the entry of several new providers using PCS and SMR spectrum undoing the cellular duopoly. Six nationwide or nearly nationwide mobile service networks have developed in addition to various regional carriers. These networks belong to Verizon Wireless, Cingular Wireless, AT&T Wireless, Sprint PCS, Voicestream, and Nextel. At the end of 2000, 91 percent of the U.S. population had access to at least three mobile operators, while 75 percent had access to at least five operators. Wireless penetration rates are now approximately 50 percent. Prices have fallen dramatically for the past several years.

4. Data and Internet Telecommunications Services

In the U.S., Internet services are unregulated. Consumers access the Internet on a narrowband (low-speed) or broadband (high-speed) basis. There were approximately 9.6 million high speed lines in the U.S. as of June 2001, representing a 36 percent increase from the previous year. Of those, approximately 5.2 million served by coaxial cable and 2.7 million served by ADSL. The residential Internet penetration rate is approximately 60 percent. Internet backbone services are

² FCC Local Telephone Competition: Status as of June 30, 2002, Industry Analysis and Technology Division, Wireline Competition Bureau at 1 & tbl. 1 (December 9, 2002), available at www.fcc.gov/wcb/stats (AFCC Local Competition Report), and FCC Local Telephone Competition Press Release at 1 (December 9, 2002). The FCC data also showed that CLECs competing via cable telephony are growing at a slightly faster pace than the overall CLEC average: cable telephone lines increased 16 percent in the first half of 2002. Cable-telephony constitutes about 12 percent of switched access lines provided by CLECs and about 1 percent of total switched access lines.

offered by numerous carriers. AOL/Time Warner is the dominant narrowband Internet service provider with 50 percent of subscribers. There are numerous alternative ISPs.

5. Multichannel Video Programming Distribution (“MVPD ») Markets

In the U.S., landline cable television providers have long been the primary source for multichannel video programming (known as «pay TV » in Europe), which the Antitrust Division has treated as a separate market from over-the-air broadcast television. These cable providers, of which the largest are AT&T/Comcast, Time Warner, and Cox, typically operate in separate geographic areas and do not overbuild each other. There are approximately 66 million cable subscribers in the U.S. Almost all other subscribers to multichannel video programming distribution received direct broadcast satellite (« DBS ») service from either DirecTV or Echostar. These two DBS providers now have approximately 20 million subscribers and a 23 percent share of the MVPD market. While cable prices have been increasing faster than inflation in recent years, DBS prices have been fairly constant, which has contributed to those companies’ increasing subscribership and market share.

3. Antitrust Division involvement in the development of a competitive local exchange market.

The Division has committed significant time and resources to the implementation of the Telecommunications Act. In 1996, the Department filed extensive comments with the FCC as it promulgated implementing regulations; the Department made recommendations regarding the unbundling of telecommunications network elements and the pricing for these UNEs.³ Department staff have advocated both formally in speeches and informally that state regulatory authorities and other interested parties adopt and advocate policies that will encourage the development and maintenance of competition. The Department also monitors the status of the local markets in anticipation of Bell company section 271 applications to ensure that our evaluations of those applications are complete. Particularly at the beginning of the 271 process, Department advocacy included speeches regarding how that process should be run, including recommendations that state regulatory authorities should begin their inquiries well in advance of an actual 271 application in order to generate a full and complete record to support the state’s, and the Department’s, evaluations (both of which must be submitted to the FCC toward the beginning of the 90-day process).⁴ The FCC agreed with this recommendation and opined that it would give greater deference to a state opinion of a 271 evaluation that was supported by such a record; more recently, the FCC has urged the states to submit their decisions even before the states’ Day 20 filing deadline.

³ Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended, and Regulatory Treatment of LEC Interexchange Service Originating in LEC’s Local Exchange Area, (August 30, 1996) available at www.usdoj.gov/atr/public/comments/1138.htm. The FCC’s Notice of Proposed Rulemaking (NPRM) permits any interested party to file comments; the Department did not have a special statutory role in this NPRM. The Department has commented on other FCC NPRMs including the 2001 NPRM on proposed performance measurements and benchmarks for wholesale local telecommunications service.

⁴ See e.g. Bell Operating Company InterLATA Entry, (July 22, 1996) available at www.usdoj.gov/atr/public/speeches/speech_turetsky.htm.

Bell companies' section 271 applications are typically thousands of pages in length. The Department submits to the FCC a formal written evaluation of each 271 application approximately 35 days into the statutorily-mandated 90-day process. From 1996 through 2002, the Department evaluated 31 Bell 271 applications covering 36 states. As of December 31, 2002, the FCC had granted 271 authority in 35 states.⁵

Since the earliest section 271 applications, the Department has advocated that in-region long distance authority is appropriate only when the local telephone market in the particular state has been « fully and irreversibly open to competition. »⁶ This standard is intended to promote the development of local competition by encouraging the cooperation of the Bell companies in opening their local markets to competition. As the FCC's own articulated standards for approval of section 271 applications match the Department's in critical respects, it has no longer proved necessary to reiterate and further refine the Department's analysis with additional economic affidavits; instead the focus has shifted to applying the « fully and irreversibly open » standard in the analysis and written evaluation of Bell company 271 applications. The Department places great emphasis on whether the Bell company has shown that it is capable, at the time of application, of providing the wholesale inputs (interconnection, unbundled network elements, and total service resale) required by the Act.⁷ In response to this consistent advocacy (and after Department opposition to and FCC denial of several initial 271 applications), the Bell companies have taken the requisite local market-opening steps in many of their states, including the implementation of forward-looking cost-based wholesale pricing for unbundled network elements, the development of complex, automated operations support systems (« OSS ») to permit prompt and reliable ordering, provisioning, maintenance and billing of these wholesale inputs, and the development of wholesale performance measurement systems to aid competitors

⁵ Some applications were initially denied by the FCC or withdrawn by the Bell company and later refiled; some applications were for more than one state. The Department's 271 Evaluations are available at <http://www.usdoj.gov/atr/public/comments/sec271/sec271.htm>. Information on the section 271 process, including FCC 271 orders, is also available on the FCC's website: www.fcc.gov/Bureaus/Common_Carrier/in-region_applications/.

⁶ The Telecommunications Act of 1996 had permitted the Department to apply any standard the Attorney General considers appropriate in evaluating section 271 applications. In its initial evaluations, the Department submitted affidavits from an expert economist supporting its chosen standard. Affidavit of Dr. Marius Schwartz: Competitive Implications of Bell Operating Company Entry into Long Distance Telecommunications Services, May 14, 1997 (attached to the Department's Evaluation of SBC's 271 Application for the state of Oklahoma), available at www.usdoj.gov/atr/public/comments/sec271/sbc/affiwp60.htm; Supplemental Affidavit of Marius Schwartz: The Open Local Market Standard for Authorizing BOC InterLATA Entry: Reply to BOC Criticisms, November 3, 1997 (attached to the Department's Evaluation of BellSouth's 271 Application for the state of South Carolina), available at www.usdoj.gov/atr/public/comments/sec271/bellsouth/1281.htm.

⁷ The Department evaluates whether the local exchange market is fully and irreversibly open to competition using all three statutorily-required modes of entry: collocation and interconnection (for CLECs offering fully facilities-based entry), unbundled network elements (for CLECs using some or all of the BOC's facilities), and total service resale. Recently filed Department evaluations have discussed problems with the Bell company's manual processing of wholesale orders, the provision of electronically auditable wholesale bills, the provision of directory listings for competitors' end-user customers, the reliability of the Bell company's performance measures and the adequacy of the processes by which changes to the Bell's OSS are planned and implemented (Change Management). Pricing for wholesale inputs has also been discussed.

and regulators in monitoring and maintaining Bell company behavior even after long distance entry is authorized.

4. Antitrust Division involvement in the development of a competitive multichannel video programming distribution ("MVPD») market.

In contrast to the primarily regulatory nature of the Division's competitive local telephony advocacy since 1996, the Division's involvement in the MVPD market during this time has involved more traditional antitrust investigation and litigation.⁸ In 1998, the Division sued a consortium of cable providers to enjoin their acquisition of the only remaining high-power orbital satellite slot capable of distributing a nationwide package of video programming competitive with cable television. In 2002, the Division sued the two most significant DBS providers to enjoin their merger. Both antitrust suits were filed in Federal District Court. In the end, the parties to both transactions abandoned the deals.

The 1998 «Primestar » case involved the proposed acquisition by a consortium of five of the largest cable companies in the United States of the only remaining high-power orbital satellite slot with full continental United States («CONUS ») coverage. While the Primestar consortium had provided a medium-power satellite television service, its owners had developed plans to implement high-power service using the full CONUS slot. This DBS service would have been competitive with cable television in the MVPD market. The Department's complaint alleged that the defendants wanted to acquire the last orbital slot because the cable companies «recognize[d] the magnitude of this competitive threat [that DBS posed to the dominant cable companies] and [sought] to "nip it in the bud," to protect their dominance and monopoly profits for years to come. » After suit was filed in the United States District Court, the deal was abandoned. Although the Primestar company never implemented the planned DBS service, it sold its assets to Hughes/DirecTV, and the remaining high-power satellite slot was sold to Echostar.

On October 31, 2002, the Division sued to block the merger of Hughes/DirecTV and Echostar, the only two high-power DBS providers with full CONUS coverage.⁹ The complaint defined an MVPD market consisting of cable and DBS providers and alleged that the proposed merger would tend to substantially lessen competition in the MVPD market across the United States reducing the number of competitors in most markets from three to two and, in markets where no cable service is available (predominantly rural areas of the United States) would create a monopoly MVPD provider. Within two months after suit was filed, the parties abandoned their merger agreement.

⁸ The Division has also filed MVPD-related sets of comments with the FCC during this time period. See *e.g.* AMCI Telecommunications Group and Echostar 110 Corp. (Jan. 4, 1999) (related to the sale of satellite spectrum to Echostar following the collapse of the Primestar II case), available at <http://www.usdoj.gov/atr/public/comments/2173.htm>; and *In the Matter of Implementation of Section 11 of the Cable Television Consumer Protection and Competition Act* (Feb. 19, 2002) (related to the FCC's cable cap proceeding), available at <http://www.usdoj.gov/atr/public/comments/10086.htm>.

⁹ The FCC was reviewing the Echostar/DirecTV merger at the same time as the Division and moved to refer the matter for hearing on public interest/competitive grounds -- effectively stating its intent to deny the necessary license transfers.

4. COMPETITION ADVOCACY IN ENERGY INDUSTRIES

Introduction

In Winter 2003-2004, the ICN surveyed several of its members regarding their competition advocacy efforts in the energy industries. Members were asked to (1) describe the structure of the energy industries in their country, (2) identify their competitive objectives and any legislation or regulations designed to further those objectives, (3) identify the source of authority for them to engage in competition advocacy, (4) identify and illustrate their advocacy efforts over time, and (5) assess the effectiveness of their advocacy efforts. Responding members included the Australian Competition and Consumer Commission (“ACCC”), the French General Directorate for Competition, Consumer Affairs and Fraud Control (“DGCCRF”), the Japan Fair Trade Commission, the Federal Competition Commission of Mexico, the Slovak Republic Antimonopoly Office, the Swiss Federal Competition Commission, and the competition authorities of the United States. This document summarizes the results of the survey and includes the member country responses. It is intended to serve as a reference of practical experience regarding competition advocacy in energy industries.

Competition Advocacy Encompasses a Wide Range of Activities

“Competition advocacy” generally refers to those activities conducted by a competition authority related to the promotion of a competitive economic environment by means of non-enforcement mechanisms, mainly through relationships with other governmental entities and by increasing public awareness of the benefits of competition.¹ As this definition suggests, and as the following country summaries reveal, competition advocacy encompasses a wide range of activities. In the energy industries, they range from educating consumers and legislators about the benefits of restructuring formerly regulated or state-operated industries, to drafting restructuring legislation, to intervening in quasi-judicial proceedings.

Advocacy Efforts Depend on Competition and Regulatory/Institutional Structures

Variations in advocacy efforts are the result of many factors, including the state of competition in an industry as well as the regulatory and institutional environment in which an industry operates. As the following summaries show, the state of competition in the energy industries ranges widely across countries from state- or privately- held monopoly, as in the case of Mexico’s oil extraction industry, to largely deregulated competition, as in the case of the United States’ oil extraction industry. Moreover, the regulatory and institutional environment varies widely across countries. In Mexico, for example, the Ministry of the Economy, an executive department, has exercised its authority to impose regulated prices on the Mexican retail LP gas industry; in Australia, on the other hand, wholesale electricity prices are determined by the interaction of buyers and sellers in auction and bilateral markets with market rules administered, in part, by the Australian Competition and Consumer Commission, an independent competition and regulatory authority.

¹ See ICN ADVOCACY WORKING GROUP, ADVOCACY AND COMPETITION POLICY (2002) <<http://www.internationalcompetitionnetwork.org/advocacyfinal.pdf>>.

Effect of Regulatory Institutions on Advocacy Efforts

Regulatory institutions will vary, in part, as the degree of competition varies across countries. Although competition may obviate the need for certain kinds of regulation, it may require other kinds of regulation. For example, regulatory institutions designed to oversee state-owned or private monopolies may be primarily concerned with establishing an appropriate price for gas or electricity in a transparent way. Regulatory institutions in a newly-liberalized market, on the other hand, might be designed to ensure that former monopolists do not abuse their incumbency. Finally, in a fully-competitive market, regulatory institutions might be designed to adjudicate the lawfulness of specific competitive practices. The advocacy efforts of a competition authority will, of course, depend on the types of regulatory institutions in place: advocating for transparency in price determination, for example, may be a pointless exercise in a competitive market where prices are determined by the interaction of many buyers and sellers; similarly, advocating for a rule to curb a specific anticompetitive practice may be pointless in a state-owned monopoly that is fully regulated.

Effect of Degree of Competition on Advocacy Efforts

Advocacy efforts by a competition authority also will depend, in part, on the state of competition in an industry. In countries that are just beginning to privatize and restructure their energy industries, competition advocacy efforts often are focused on building a consensus in favor of competition by educating legislators and consumers regarding the benefits of competition. In the Slovak Republic, for example, the Antimonopoly Office drafted legislation designed to create a more unified regulatory structure; in Mexico, the Federal Competition Commission has evaluated and offered its opinion on electricity and gas reform proposals; and in Switzerland, the Federal Competition Commission issued opinions on recent legislation to liberalize the electricity sector.

In energy industries that have begun to open to some degree of competition, advocacy efforts tend to be less focused on advocating for basic reform and more focused on ensuring that new legal and institutional structures are designed to maximize the benefits of competition. In Japan, for example, the Fair Trade Commission has published a report on how to encourage more entry into the electricity sector; and in France the Competition Council has advocated a series of steps designed to ensure that state-owned companies operate like private enterprises in the electricity sector.

In energy industries that have been open to competition for some time, advocacy efforts often are focused on cooperating with other government agencies responsible for competition matters to ensure that advocacy efforts are as efficient and as effective as possible. Competition authorities in countries with established competitive industries also intervene in established regulatory and quasi-judicial processes to promote rules that are consistent with competition. In Australia, for example, the Competition and Consumer Commission established a forum bringing together state, territory and industry-specific regulators to promote information sharing and consistent policy development; in the United States, the Department of Justice and the Federal Trade Commission have frequently participated in regulatory and adjudicative proceedings before energy regulators.

General Advocacy Efforts

There are, of course, several types of advocacy that can be useful regardless of the degree of competition in, or regulatory institutions governing, an industry. Almost all competition authorities in this survey have engaged in efforts to educate legislators, regulators, and the public regarding the benefits of competition. Indeed, almost all have advised lawmakers on energy-related legislation. The Federal Competition Commission of Mexico, for example, analyzed and commented on electricity reform legislation put forward in 1999 and 2002. Providing such advice to legislatures is sometimes required by statute, as in the case of Switzerland; sometimes it is merely permitted by statute, as in the case of the Competition Council in France and the Federal Trade Commission of the United States. Many of the competition authorities in this survey have appeared at public forums to promote competition. In Australia, for example, the Chairman of the ACCC, other commissioners, and senior staff speak on utility regulation at various conferences and public forums. And many competition authorities have cooperated with other regulators responsible for competition policy. In the United States, for example, the competition authorities have regular meetings with other national-level agencies interested in regulatory reform. In France, the DGCCRF has cooperated with the European Commission to negotiate an acceptable resolution to a transnational electricity merger. Finally, many have published research or other works advocating competition and aimed at regulators, legislators and the public. For example, the ACCC publishes articles and studies dealing with the specifics and rationale of its work.

The Effectiveness of Advocacy

The results of this survey suggest that it is difficult to assess the effectiveness of advocacy efforts because it is difficult to distinguish the effect of those efforts from the many other factors that affect policy. In some cases, however, it appears that substantial public or political opposition can render advocacy efforts moot. For example, Mexican Government, including competition authorities, have run into political opposition to reform from political parties and unions that delayed or deterred procompetitive policies; and Swiss competition authorities have run into public opposition as expressed in a referendum that voted down electricity market reform. Nonetheless, it appears that even when advocacy fails to produce a preferred policy result in the short run, advocacy efforts can have a long run effect by creating an environment in which the benefits of competition are widely understood and competition itself considered desirable. For example, advocacy efforts in the United States stressing the importance of structural rather than behavioral remedies for anticompetitive outcomes have, independent of their direct effect on policy, fostered an environment in which other regulatory agencies could focus on structural remedies.

Conclusion

The following country summaries describe a wide range of competition advocacy efforts in the energy industries. Some advocacy efforts – such as publishing studies and reports about the benefits of introducing competition, participating in public forums regarding competition policy, and cooperating with other regulatory authorities – are useful in any environment. The usefulness of other advocacy efforts may depend on the regulatory and institutional structures – as well as the degree of competition – in place. The effectiveness of advocacy efforts in producing a particular procompetitive policy outcome in the short run may be limited by public

and industry opposition. In the long run, however, it appears that competition advocacy is effective when it contributes to an environment in which the benefits of competition in the energy industries are widely understood.

4.1. AUSTRALIAN COMPETITION AND CONSUMER COMMISSION



INTERNATIONAL COMPETITION NETWORK

ADVOCACY WORKING GROUP SUBGROUP III – SECTOR STUDIES

Energy Sector: Australia

Introduction

Australia is a federation. It has a Commonwealth government, six self-governing states and two self-governing territories and more than 700 local governments.

The competition agency in Australia is the Australian Competition and Consumer Commission (the ACCC) which is a Commonwealth independent statutory body responsible for administering the *Trade Practices Act 1974* (Cth) (TPA)¹. The ACCC also has the role of economic regulator for gas and electricity transmission networks as well as for telecommunications and transport infrastructure. The ACCC's powers and functions include investigating possible breaches of the competition and consumer protection provisions of the TPA and, where appropriate, bringing legal proceedings against those the ACCC considers to have breached the TPA.

The purpose of this paper is to provide the ACCC's experience in competition advocacy within the Australian energy sector to a subgroup of the International Competition Network (ICN) Advocacy Working Group. The Advocacy Working Group has a mandate to undertake projects with a view to recommending best practices to ICN members and to provide them with information to support their advocacy task.

Background

In 1990, as part of the Commonwealth Government's commitment to micro-economic reform, the Industry Commission² (IC) was requested by that Government to undertake an inquiry into the efficiency of the generation, transmission and distribution of electricity and the transmission and distribution of gas.

In 1991 the IC produced their Report entitled *Energy Generation and Distribution*. The Report recommended a major restructuring of the Australian electricity and natural gas supply industries to increase competition and thus efficiency.

In relation to promoting competition in the electricity industry, the IC recommended:

- the unbundling of the generation, transmission and distribution functions;
- the dividing of the distribution and transmission sectors in order that there be several bodies to compete for market share;
- progressively privatising public utilities involved in generation, and distribution;
- that one national body should be responsible for all transmission functions (apart from Western Australia and the Northern Territory³) so that there can be one integrated Australian electricity market; and
- to reduce the potential for abuse of market power, that transmission and distribution utilities be required to provide open access.

In relation to promoting competition in the gas industry, the IC recommended:

¹ The ACCC is made up of a Chairman and Commissioners nominated by the Commonwealth and endorsed by a majority of states and territories.

² A Commonwealth economic research agency.

³ Due to geographical reasons.

- removing State barriers to interstate trade in natural gas;
- separation of gas transmission and distribution functions;
- increased competition in distribution;
- progressively privatising public utilities involved in distribution; and
- to reduce the potential for abuse of market power that transmission and distribution utilities be required to provide open access.

As an extension of the micro-economic reform agenda, in 1991 the Council of Australian Governments⁴ (COAG) being the Prime Minister, Premiers and Chief Ministers of the Commonwealth, State and Territory Governments agreed to examine a national approach to competition policy. The first step in this process was the establishment in the following year of the National Competition Policy Review by a committee chaired by Professor Fred Hilmer.

On completion of the Hilmer Committee's Report in August 1993, the Commonwealth, State and Territory Governments began extensive negotiations on implementation of its recommendations. The recommendations made by the Hilmer committee were generally accepted by COAG in April 1995 and the processes culminated in the Competition Policy Reform Act 1995 which when coupled with three inter-governmental agreements (the Competition Principles Agreement, the Agreement to Implement the National Competition Policy and Related Reforms and the Competition Code Agreement), resulted in a number of wide ranging reforms.

In introducing these reforms governments recognised that while tariff reductions had opened the traded goods sector to competition the provision of services by public utilities and a number of other sectors of the economy remained sheltered from international and domestic competition. Similarly there was a growing understanding of the needs of exporting and import competing businesses. If Australia is to compete effectively in the international economy it needs an efficient non traded sector to reduce input prices to business.

A central reform was the agreement to apply competition laws to all businesses regardless of ownership. Until then there was some uncertainty as to the application of the TPA to certain government business enterprises (GBEs), and the TPA did not apply to unincorporated businesses, partnerships and professional bodies. Now the provisions of Part IV of the TPA or the equivalent provisions, which apply by virtue of the Competition Code application legislation in each state and territory, cover everyone.

Broadly speaking, Part IV of the TPA prohibits the following anti-competitive practices:

- Anti-competitive agreements and exclusionary provisions, including primary or secondary boycotts (s.45);
- Misuse of market power (s.46);
- Exclusive dealing (s.47);
- Resale price maintenance (ss.48, 96-100); and

⁴ The role of COAG is to initiate, develop and monitor the implementation of policy reforms which are of national significance and which require cooperative action by Australian governments.

- Mergers, which would have the effect or likely effect of substantially lessening competition in a market (ss.50, 50A).

Another central reform from the Hilmer Report recommendations was the introduction of Part IIIA into the TPA⁵. At the time Part IIIA was seen as being a revolutionary step in competition policy in that it introduced to the Australian economy a general access regime which established rights of access to ‘essential facilities’⁶ for competitors operating upstream or downstream from such facilities.

Access to the electricity transmission and distribution networks in the National Electricity Market (NEM), and access to gas pipelines is addressed through Part IIIA⁷. Part IIIA is an integral part of competition law as it addresses the market power of infrastructure bottlenecks through mandatory access provisions. Such access is essential if there is to be competitive production and retail markets in electricity and gas.

In 1994, COAG agreed to remove all remaining legislative and regulatory barriers to free and fair trade in gas and electricity, and to implement complementary legislation.

In relation to gas, in February 1994, at the Hobart meeting of COAG several principles were agreed relating to the introduction of free and fair trade in gas by July 1996. These principles included:

- The removal of all remaining legislative and regulatory barriers to free trade of gas by July 1996;
- The implementation of complementary legislation so that a uniform national framework would apply to third-party access to all gas transmission pipelines within and between jurisdictions by July 1996; and
- The introduction of legislation to ring-fence transmission and distribution activities in the private sector.

The task of developing a uniform national framework for third-party access to all gas transmission pipelines was assigned to the COAG Gas Reform taskforce in June 1995. After several rounds of consultation, the task force’s successor organisation, the Gas Reform Implementation Group (GRIG), submitted such a framework to the governments. This document, the Natural Gas Pipelines Access Inter-Governmental Agreement (IGA) was signed by the prime minister and the premiers and chief Ministers of all states and territories on 7 November 1997.

The IGA constitutes a binding commitment by the governments to adopt legislation for open access. It also contains the legislative, administrative and transitional arrangements for

5 The Hilmer Committee accepted that existing legislative measures to address access to essential facilities or access pricing problems were inadequate. The limitations of s.46 (misuse of market power) of the TPA had been well documented. These include the problem that the provision is only available ex post, and that courts must infer intent. The limited suitability of the *Prices Surveillance Act 1983* as a means to address access related disputes was also acknowledged by the Committee.

6 Following the North American usage, “essential facilities” are normally understood to be services with natural monopoly characteristics, access to which is required by participants in upstream or downstream markets to be able to compete effectively in those markets. Access problems can be of particular concern where public utility monopolies are vertically integrated into competitive markets and are able to limit competition in these markets by restricting access to the essential facility services.

7 Attachment I provides a discussion on Part IIIA.

implementing the national regulatory regime. The national access regime is made up of the access legislation and the National Third Party Access Code for Natural Gas Pipeline Systems (the Code). Legislation and the Code define the rights and obligations of pipeline operators and users that apply for third party access to natural gas transmission pipelines and distribution networks. They do not cover upstream facilities.

In relation to electricity, the National Grid Management Council (NGMC) was created by COAG in response to the IC's Report to develop arrangements for a competitive national electricity market. COAG agreed that the national electricity market would be governed by a Code of Conduct to be developed by the NGMC.

The main objectives of a fully competitive electricity market agreed to by COAG at its 19 August 1994 meeting are:

- The ability for customers to choose which supplier, including generators, retailers and traders, they will trade with;
- Non-discriminatory access to the interconnected transmission and distribution network;
- No discriminatory legislative or regulatory barriers to entry for new participants in generation or retail supply; and
- No discriminatory legislative or regulatory barriers to interstate and/or intrastate trade.

NGMC developed these objectives into a code of conduct, the National Electricity Code (NEC) that establishes the rules by which each NEM participant must abide.

The NEC was submitted to the ACCC on 15 November 1996, for formal authorisation under Part VII of the TPA. In line with COAG competition policy reforms the NEC also encompasses an access regime. Accordingly on 28 April 1997, the NEC was submitted to the ACCC for approval as an industry access code under Part IIIA of the TPA. The ACCC authorised the NEC on 10 December 1997 and the NEM started on 13 December 1998.

As an incentive to the state governments to accelerate the implementation of the competitive reforms to their previously closed energy industry, the Federal Government decided to pay 'competition payments' to the states and territories totalling A\$4.2 billion up to 2005-2006. Payments are conditional, in part, on the satisfactory implementation of electricity supply and gas industry reforms.

An outcome of the COAG reform process of the 1990s was the establishment of the ACCC as the national competition body responsible for the administration of Australia's competition laws and the national utility regulator.

The ACCC - Competition Advocate

Why is the ACCC involved in competition advocacy?

The ACCC is an independent statutory authority charged with administering the TPA. The ACCC's experience and belief is that in order to promote competition and thereby economic efficiency it is beneficial for it to play a competition advocacy role in addition to administering the TPA.

The ACCC's independence as a statutory authority as well as its expertise in both competition and economic regulation provides it with the imprimatur it requires in performing this advocacy role.

Whilst in Australia the development of policy or legislation in specific sectors is the responsibility of the Government, as regulation of energy markets can have a substantial impact on competition in markets, the ACCC as an independent statutory authority can usefully contribute to all levels of debate.

Against the ACCC's independence - arguments by regulated businesses may appear self serving and captured by sectoral interest. For example when regulated companies state that the regulatory framework and its implementation is deterring investment it is obvious that it is in the commercial interests of such companies to present arguments that are not in the best interests of economic efficiency, such as arguing for higher regulated prices.

As mentioned earlier the ACCC is the economic regulator for electricity and gas transmission networks as well as for telecommunications and transport infrastructure. As many of the regulatory issues are similar the multi-sector agency is able to apply lessons learnt in one infrastructure industry across others. This broad perspective is valuable in the application of pricing principles and other regulatory matters across sectors.

The ACCC in addition to regulating a number of infrastructure industries is also the competition regulator. Combining the functions of competition and economic regulator means the ACCC can bring a strong competition focus to the policy debate on energy regulation in Australia. Competition agencies tend to be more attuned to the benefits of competition, what constitutes a competitive market and what threatens it.

As a multi-sector regulator⁸ the ACCC has a clear perspective on which services should and should not be regulated. Where it is considered no longer necessary the ACCC has removed regulation. This would be less likely if the regulator were industry specific and more likely to be captured by sectoral interests. For example in the telecommunications sector last year the ACCC ceased regulation of local call services in major capital cities in Australia. The decision by the ACCC was based on its expert judgement as both competition and economic regulator of the telecommunications sector that the developments in competition within that sector of the market meant that improved market outcomes would be achieved with less regulation.

In some markets competition may not be possible and the ACCC would likely advocate in favour of regulation. This has been the case in some segments of the Australian energy sector where there have been significant economies of scale and barriers to entry. In this case a system of regulation for gas pipelines and electricity transmission and distribution is critical to achieve a fully integrated energy market that delivers reliable and efficiently priced energy.

An important aspect of the advocacy function is spelling out the implications of public policies for competition and efficiency so that government decision making takes them into account. All Australians are entitled to be informed on the effects of competition and how the benefits of informed markets impact on them as businesses and consumers. A more informed community

⁸ Attachment II provides a discussion on multi-sector regulation versus single sector regulation.

leads to a greater level of debate and heightened awareness of the advantages of competition and efficient markets for the community as a whole.

How is the ACCC involved in competition advocacy?

The ACCC in its advocacy role seeks to provide advice, influence and participate in government economic and regulatory policies in order to promote more competitive industry structures, firm behaviour and market performance. It achieves this through: Assisting in the formulation of public policies; Use of the media; Enforcement and Competition advocacy; Speeches on utility regulation to various organisations as well as publications such as guides to various aspects of utility regulation; Briefings to relevant Ministers and members of Parliament; Appearances before the Senate Estimates Committee as well as other bodies such as the Commonwealth ombudsman, the Administrative Appeals Tribunal, the Australian Competition Tribunal and various consultative committees; International activities; and Incentive based regulation.

- *Assisting in the formulation of public policies:*

The ACCC by virtue of its 30 years experience as both competition and economic regulator is able to assist in the formulation of public policy by providing both detailed and high level submissions and policy advice on energy related matters⁹.

The ACCC has recently been involved in several reviews involving aspects of competition and economic regulation of the Australian energy sector. Indeed much of the framework governing the ACCC's economic and regulatory work has been recently reviewed or is currently being reviewed. The ACCC regards its participation in these reviews as being of the utmost importance because they give all parties an opportunity to comment on the existing framework with the aim of refining their future implementation.

The COAG Energy Market Review

In December 2002 COAG commissioned an independent review into energy market reform. The Energy Market Review's final report recommends significant further reform of Australia's electricity and gas markets. These include structural reform of energy markets, reform of governance arrangements, and measures to improve electricity and gas transmission investment outcomes.

The broad aims of the Review are to improve the operation and efficiency of energy markets and to complete the move from fragmented state based markets to genuinely national markets. The reforms proposed would build on those reforms undertaken since the early 1990's.

⁹ As a multi-sector agency, the ACCC is able to provide the gas and electricity industries with the following benefits:

- gas and electricity transmission regulation currently benefit from the ACCC's role as a multi-sector regulator covering telecommunications, rail, and aviation. The ACCC maintains regulatory expertise across several sectors, leading to better and more predictable regulatory outcomes;
- 30 years of comprehensive experience in investigation and enforcement of Part IV of the Trade Practices Act 1974 as well as invaluable corporate memory; and
- the ACCC is able to take advantage of the synergies gained in applying both the regulatory work of the ACCC and the broader competition law enforcement. Decisions can be taken in full understanding of the current state and future direction of the market as well as the interaction between broader competition laws

While over the past few years the governance arrangements in the energy sector have proved workable in delivering reforms in the electricity and gas sectors, the ACCC has agreed that further reforms are required.

Many of the reforms required are independent of the regulatory governance issues. For example the current arrangements do not reserve NEM policy decisions to governments, nor provide adequate means by which participating jurisdictions can provide policy oversight and direction to guide the development of the market.

Eight agencies are involved in economic regulation of the NEM (NECA, the ACCC and the jurisdictional regulators). As well, the jurisdictions themselves are involved in various aspects of the development of the market and NEMMCO is responsible for the operation of the wholesale electricity market and technical regulation.

Responsibility for the economic regulation of gas pipelines is split between the ACCC and jurisdictional regulators. Multiple energy regulators raise the risk of inconsistent decisions and an uncertain regulatory environment arising from diverging directions amongst the many regulators. Regulatory institutions have attempted to address this issue administratively through the establishment of the Regulators Forum and through the Energy Committee of the ACCC.

The current arrangements diffuse responsibility for oversight of the energy market and energy regulation. They also make the electricity code change processes complex and slow.

Regulatory fragmentation is of real concern under the current governance arrangements. It is vital that any change to the governance arrangements does not simply shuffle regulatory responsibilities between agencies.

Over the past few months much of the debate about electricity market reform has focussed on the institutional arrangements for regulating the energy sector. The ACCC is concerned that the focus on changing institutional arrangements could obscure the reality that the drivers of reform in energy markets are policy decisions, not the make-up of institutions themselves. This is not to say that the current institutional arrangements cannot be improved however any changes need to be carefully considered.

While the objective of reform is to create a national energy market and to recognise the legitimate policy role for governments within that national market, any meaningful reform needs cooperation between State and Commonwealth governments.

The ACCC has provided three submissions to this Review. In addition the Chairman of the ACCC and senior representatives has appeared before the Review Committee to provide additional advice when necessary.

Currently the Commonwealth is preparing its response to the COAG Energy Market Review. The Minister for Industry's Department has been charged with formulating the Government's response. This will be done with the oversight of a high level interdepartmental committee, the Prime Minister's taskforce on energy as well as a cabinet sub committee chaired by the Prime Minister and comprising the relevant Ministers of each Department.

The ACCC has an ongoing role in the formulation of the Commonwealth's response by providing advice to the Department of Industry on both economic regulatory issues in relation to the electricity and gas markets as well as on competition issues.

National Electricity Market (NEM) Ministers Forum

The NEM Ministers Forum is currently reviewing a model for a single energy regulator. It is envisaged that the Review will be dovetailed into the Commonwealth's response to the COAG Energy Market Review. The ACCC has provided a submission to this Review. In addition the Chief Executive Officer, the Executive General Manager of Regulatory Affairs Division as well as other senior staff have appeared before the Forum in order to present the arguments contained in the submissions and to be able to clarify questions that the Ministers may have in relation to the institutional arrangements within the Australian energy sector.

Part IIIA Review

After five years of operation the Commonwealth Government requested the Productivity Commission¹⁰ to undertake an inquiry into the operation of part IIIA. As discussed above the access regime is one part of a package of pro-competitive reforms adopted by COAG in April 1995. Access is an important element in the competition reform program. Without access the other measures will not always be sufficient to ensure benefits in terms of competition and efficiency. The ACCC made a comprehensive submission to the PC's Inquiry. This submission contributed to the Commonwealth Government's support for the PC's recommendation that Part IIIA be retained.

- *Use of the media*

The ACCC as with all regulators is accountable to the public in many ways. The public has the right to know about the TPA and how the ACCC enforces it. Parliament's intention in this regard is reflected in section 28 of the Act, which obliges the ACCC to publicise the TPA and its work. The TPA is an important, far reaching law intended to promote the welfare of all Australians. All Australians are entitled to know how the TPA affects their rights, their obligations and their welfare, to know how it is being implemented. Making the public aware also builds public confidence in the law and its administration, and enables informed debate and criticism of its shortcomings.

The media therefore has a vital role in disseminating important information to the public and the business community, and in provoking debate about the law. Economic and competition reform of the energy sector is not an area usually the subject of media attention, and so the ACCC has worked hard to ensure that the benefit of competition in these sectors is more widely known in the community. The ACCC has found that the most effective and efficient way to bring matters to the attention of the public is by issuing media statements.¹¹

Media coverage and scrutiny of the ACCC's activities also plays a significant role in ensuring that the ACCC is transparent. By consulting widely, describing its processes and explaining its decisions, the ACCC maintains its transparency. It is very clear to the ACCC that it cannot be accountable without also being transparent.

¹⁰ A research body. Formally known as the Industry Commission (IC).

¹¹ Attachment 3 provides examples of ACCC media releases in relation to competition and economic regulatory decisions made by the ACCC in relation to the gas and electricity sectors.

The publicity accorded to competition and consumer protection law and its regulators has increased in most countries, reflecting greater activity by regulators and the greater importance of their activities to their countries economies.

- *Enforcement and Competition advocacy:*

The ACCC's advocacy work usually revolves around its responsibilities under the TPA. Advocacy is closely linked to enforcement activity, and so the promotion of competition in general is often achieved through the dissemination of information about a particular action.

Publicising competition issues makes the task of competition advocacy easier. Publicity plays an important role in achieving compliance with the TPA through dissemination of information to businesses and the public. Releasing information through the media promotes compliance by example and illustrates the consequences of breaching the TPA.

For example in 2002 following action by the ACCC,¹² the Federal Court ordered penalties of \$14.5 million against Schneider Electric (Australia), Wilson Transformer Company and AW Tyree Transformers for their involvement in price-fixing and market-sharing arrangements in the power transformer and distribution transformer markets. Alstom Pty Ltd was previously fined \$7 million for price fixing.

The transformer market is a significant Australian market, estimated to be worth \$160 million per annum. The unlawful conduct by these companies, and by these executives places upwards pressure on prices – directly disadvantaging producers and businesses and families in regional areas.

- *Speeches on utility regulation to various organisations as well as publications such as guides to various aspects of utility regulation:*

The ACCC makes available its Chairman, other commissioners, and senior staff to speak on utility regulation at various conferences and public forums throughout any given year¹³.

The ACCC has a very active publications program dealing with the specifics and rationale of its work¹⁴. This includes a regular journal of developments and issues, and a wide range of booklets, guidelines and discussion papers aimed at promoting better understanding of the legislation for which the ACCC is responsible, its work and procedures¹⁵.

- *Briefings to relevant Ministers and members of Parliament:*

The Chairman, commissioners, chief executive officer and other senior staff of the ACCC are continuously involved in providing briefings and both written and verbal advice to the Government and to other members of Parliament. Given the ACCC's independence as a statutory

12 This media release is provided in Attachment 3.

13 Attachment 4 provides examples of speeches made by the Chairman, commissioners and senior staff on utility regulation.

14 Attachment 5 provides examples of publications on various aspects of utility regulation.

15 Many of these publications are available to the public at the ACCC's Internet website - <<http://www.accc.gov.au>>

authority frequently members of parliament call on the ACCC to provide their expert advice on both competition and economic issues.

During the course of the COAG Energy Market Review the ACCC frequently provided advice to members of parliament both State and Federal on issues both specific and general that related to the public debate on energy markets in Australia.

- *Appearances before the Senate Estimates Committee as well as other bodies such as the Commonwealth ombudsman, the Administrative Appeals Tribunal, the Australian Competition Tribunal and various consultative committees:*

The ACCC must be prepared to explain its actions to the above mentioned bodies as the taxpayer is entitled to a full explanation of how the ACCC's budget is being spent, as are relevant Ministers and parliament.

Quite often when the ACCC is explaining its actions to one of the above mentioned bodies the ACCC Chairman, commissioner, chief executive or senior staff member will take the opportunity to put on the public record the ACCC's view in relation to a matter of public policy. In this way the ACCC is accountable to Parliament and helps inform policy makers of its reasons.

- *International activities:*

The ACCC's international activities are aimed at helping other countries achieve effective competition and consumer protection regimes. This can mean more competitive and fairer overseas markets and better access to those markets for Australian exporters.

The ACCC is increasingly cooperating with its international counterpart agencies on competition, consumer protection and regulatory matters to facilitate the effective enforcement of laws both in Australia and overseas.

One avenue through which this is occurring is the recently established international Competition Network (ICN), a global forum through which individual competition agencies are liaising on common issues.

- *Incentive based regulation:*

The ACCC's view is that its regulatory work provides a favourable environment for investment in gas and electricity transmission infrastructure. The ACCC's decisions provide earnings opportunities comparable to that elsewhere on the Australian share market¹⁶.

The incentive framework encourages the regulated business to outperform the benchmark rate of return established by the ACCC for the forthcoming regulatory period. Incentive regulation gives discretion to the service provider to operate its business and allows it to benefit from returns greater than those anticipated by the regulator. The result is intended to be more efficient.

This is of particular relevance to Australia where at the commencement of regulation, many energy infrastructure assets had been government owned and there was little information about appropriate prices. Applying incentive regulation to newly privatised and corporatised businesses

¹⁶ While these figures provide a good benchmark for comparison, the differences in regulatory frameworks under which they are determined should also be considered.

has provided the opportunity for the business to move towards more efficient structures, operation and pricing over time while passing on some of these benefits to users.

OUTCOMES OF COMPETITION ADVOCACY IN THE ENERGY SECTOR

Progress of energy market reforms

Over the past decade Australian governments have undertaken wide-ranging reforms in the energy sector. The ACCC has had a role in implementing the reforms in both the gas and electricity markets.

Benefits of Reform achieved to date

The reforms introduced over the last decade have gone a long way to achieving the objectives set out by COAG. State and territory governments, in conjunction with the Commonwealth, structurally separated government owned gas and electricity utilities, established the NEM and established new institutions to manage and regulate energy markets. They also established access regimes covering electricity transmission and distribution services and gas pipelines.

The benefits are showing with a trend to more efficient electricity and gas pricing, improved service standards and substantial new investment in all parts of the energy market.

- Over \$800 million in gas transmission developments is under construction or committed¹⁷;
- A further \$5.4 billion in gas transmission investment is proposed¹⁸;
- Approximately \$800 million in inter-state electricity transmission infrastructure was completed in the last 18 months¹⁹;
- \$2.5 billion in intra-state electricity transmission was approved by the Commission covering a five year time frame (the new investment will increase the transmission asset base in the National Electricity Market by 40-50 percent); and
- a further \$700 million or so is proposed for electricity interconnection²⁰.

Nevertheless there is still some way to go before the goals set by COAG in the 1990s are achieved.

Reform process not complete

To date the reform of the electricity and gas industries are partly complete. However, despite the agreement by COAG to their implementation - reform progress has met with some resistance.

- In the electricity industry further structural reforms are needed to realise the full competitive potential of the NEM. For example the market structure of electricity generation in NSW in particular remains a concern in some jurisdictions;

¹⁷ Source: Delta Electricity & Access economics "Investment Monitor" No. 46, June 2001, p.20.

¹⁸ *ibid*

¹⁹ Queensland-NSW interconnector, Directlink, Murraylink and Snovic 400

²⁰ Basslink, South Australia NSW interconnector and Southernlink

- The gas market remains fragmented arguably because of limited inter-state pipeline transmission infrastructure;
- The NEM also remains fragmented because of inadequate transmission interconnection;
- Customer choice of supplier is still not available to many energy customers particularly in Queensland;
- The structure of the retail sector in some states remains a concern, with dominant retailers in the market. With such a retail competition framework, it will be difficult to achieve effective retail competition; and
- Differences in market governance arrangements are emerging among various states. For example prudential arrangements differ among states and there are several examples of the duplication of planning and interconnection approval processes.

The renewed interest of governments in energy policy is welcomed. The establishment of the Prime Ministers Taskforce on Energy, the COAG Energy Market Review and the NEM Ministers Forum are examples of governments' desires to resolve market issues. They provide an opportunity to complete electricity market reform.

Conclusion

This paper has provided a perspective on the ACCC's experience in competition advocacy in the Australian energy sector. The paper began by providing the background to the competition reforms of the 1990's that led to the establishment of a national energy market in Australia. This was followed by the reasons for the ACCC's involvement in competition advocacy and then how it is involved. Finally the outcomes of the ACCC's efforts in competition advocacy were examined.

Attachment 1

Part IIIA

The concept of access to essential facilities has been developed over some years in the US. The essential facilities doctrine has established:

A monopolist has no general duty to share his essential facility, although there are certain circumstances in which he must do so ... In the special circumstances where there may be such an obligation, the elements of an antitrust claim for denial of access to an essential facility are (1) a monopolist who competes with the plaintiff controls an essential facility, (2) the plaintiff cannot duplicate that facility, (3) the monopolist denied the plaintiff's use of the facility, and (4) the monopolist could feasibly have granted the plaintiff use of the facility ...²¹

The Hilmer Committee recognised that there was a need to develop access rights to 'bottleneck' facilities and promote competition in the linked competitive markets, both upstream and downstream from the facility.

In New Zealand, access to facilities falls under the misuse of market power provisions of the general competition law (s.36 of the *Commerce Act 1986*) and is reliant on court action.

However, it was the view of the Hilmer Committee that the Australian Trade Practices Act misuse of market power provisions (contained in s.46) did not include the US doctrine of essential facilities and that it would be an inadequate method for providing third party access to essential facilities.

Accordingly, in 1995 a legislated access regime was developed and set out in Part IIIA of the Trade Practices Act. There are three components to Part IIIA:

- negotiate-arbitrate. This is the basis of the regime and seeks to facilitate agreement between parties and provide an arbitration process when agreement cannot be reached. Services that are to be subject to this regime must first be 'declared' by the Commonwealth Minister. If the terms and conditions of access are not successfully determined through negotiation between the parties the dispute can be referred to the ACCC for arbitration.
- effective regimes. Part IIIA is intended to operate concurrently with other access regimes developed by the Commonwealth, state or territory governments. Where such a regime exists, it is anticipated that that regime be used in preference to Part IIIA. Accordingly, governments are able to seek recognition for their own access regimes and consequently not be subject to declaration under Part IIIA.
- undertakings. Part IIIA allows service providers to give access undertakings to the ACCC specifying the terms on which access will be made to third parties. If these undertakings are accepted the service in question cannot be declared under Part IIIA. These undertakings are enforceable through the Federal Court.

Part IIIA provides the basis for the industry specific regimes developed for the gas and electricity sectors. Details of the institutional arrangements in gas and electricity follow.

21 Caribbean Broadcasting System Ltd v Cable & Wireless plc 148 F 3rd 1080 (1998) in Miller V (ed) Miller's Annotated Trade Practices Act 1974, 23rd edition, 2002, p. 148.

Attachment II

Governance – multi-sector agencies

The ACCC believes that multi-sector regulators are superior in performance and reliability to single sector regulators. The Commission's arguments are based on its own experience as a regulator, the findings of the Hilmer Report and research by the OECD.

International trends

This view appears to be supported by recent international events. In the Netherlands, the demonstrated benefits of combining sectoral and competition regulation have led to a proposal to combine the Independent Post and Telecommunications Authority (OPTA) and the Netherlands Competition Authority (NMa). The Netherlands energy regulator (DTe) is already a division of the competition authority.

OPTA and the NMa have recently visited the Commission to enquire about the Commission's experience in competition and sectoral regulation and indicated that the Commission's regulatory model was regarded as an effective model for the Netherlands' governance arrangements.

Regarding the reasons for the merger, OPTA and NMa indicated that their responsibilities are directed towards ensuring that markets operate in the interests of both consumers and business. They believed that combining competition and sectoral regulatory functions would be the optimal means of using the regulatory tools they have available. OPTA and NMa have acknowledged their respective strengths and have stated that general and sector-specific instruments will be used in a way that results in tailor-made, effective regulation, stricter where necessary, and more restrained where possible.

In the UK, convergence of regulatory institutions has also been observed. The synergies that result from combining sectoral regulators have led to the creation of Ofgem by combining the former Office of Gas Supply (Ofgas) and the Office of Electricity Regulation (OFFER). These two offices were merged in response to growing convergence in the two industry sectors, efficiencies to be gained, and the realisation of the need to take a combined regulatory approach.

While notionally industry specific, in practice Ofgem has strong links with the competition regulator. Ofgem's decisions are appealable to the UK Competition Commission which has responsibilities similar to the ACCC. The UK model is best described as an energy regulator linked to a competition regulator. This arrangement reflects:

- the regulatory synergies to be gained by linking sector specific and competition regulation;
- the need to ensure consistency in regulation across industry sectors; and
- the need for sector specific agencies' decisions to be under review by a competition agency to ensure that a broad competition perspective informs regulation.

Lessons from financial industry regulation

An examination of the governance arrangements in Australia's financial industry is instructive in regard to the limitations of sector-specific agencies.

In the Australian context ASIC serves well as an example. ASIC's role is a co-regulator with the Commission. It has a consumer protection role in the financial industry, but does not cover authorisation assessments under the TPA, or have enforcement functions under Part IV of the TPA, all of which remain with the Commission.

In consumer protection work in the financial industry, ASIC has formally delegated the regulation of all consumer protection aspects of health insurance to the Commission. In this regard ASIC's model is a "partial" economic regulatory model, covering consumer protection issues (with some exceptions). Given the close links between the Commission's core competition work, ASIC and the ACCC have entered into a Memorandum of Understanding to establish protocols to deal with conduct that may raise issues under both the ASIC Act and the TPA.

Recent experience in insurance industry regulation suggests that sector specific regulation can leave agencies without adequate resources or experience to monitor markets and enforce laws. It is important that the lessons learned from this experience are applied in devising the optimal regulatory structure for the electricity or gas industries.

4.2. FRENCH MINISTRY OF FINANCE - DGCCRF

REGULATORY REFORM AND COMPETITION ADVOCACY IN THE ENERGY SECTOR

Introduction

Competition advocacy refers to the activities conducted by competition authorities so as to promote a competitive environment by seeking to influence other governmental entities and increasing public awareness of the benefits of competition. In France, this role is carried out by both the Competition Council ("*Conseil de la concurrence*") and the General Directorate for Competition, Consumers Affairs and Fraud Control ("*DGCCRF*").

The DGCCRF pursues these aims by discovering and analysing illegal agreements and abuses of dominant positions. It also examines mergers before proposing a decision to the Minister of Economy, Finance and Industry. Finally, it supports the opening up of regulated sectors such as air transport, telecommunications, electricity and gas to competition. In the field of electricity fares, DGCCRF regulates consumer sale tariffs, in conjunction with the Industry State Secretary and with CRE¹'s expertise.

The *Conseil de la concurrence* pursues these aims by enforcing competition rules relating to cartels and abuses of dominant positions. It also gives its opinion on mergers when requested to do so by the Minister of Economy. The Council can also be referred to in order to provide its opinion on any question of competition by the Government, parliamentary committees, local authorities, professional organisations, trade-unions or consumers.

The French competition authorities have been particularly active in the sector of energy. This paper explains how the French competition authorities have played their advocacy role by favouring better regulation and by fostering the application of competition rules.

1 The recent opening up of electricity and gas markets

Since 2000, the opening of energy markets has entailed a European wave of mergers in this sector. With the presence of new competitors on their domestic market, European undertakings seek to conquer market shares out of their former borders, particularly in countries which are electric "peninsulas", where electricity exports are difficult (Spain, Italy, the United Kingdom and Germany, the latter because of its market structure). These consolidation operations fall under mergers control at the national and European level. A striking example is EDF's acquisition of a 34% capital share in the German firm EnBW. In order to get the European Commission's clearing for this operation, EDF has committed itself to make 6000MW of its production capacities available to other electricity enterprises. The European Commission has asked DGCCRF to participate in negotiations related to EDF/EnBW transaction. As a result of these commitments, five auctions have been organised, representing 4000 MW.

¹ CRE stands for Commission de Régulation de l'Énergie, Energy Regulation Committee, the sectoral regulator.

France has achieved the first stage of liberalisation of electricity and gas markets provided for by European directives of 1996 and 1998, while putting an end to more than fifty years old monopolies.

In the **electricity sector**, the law of 10 February 2000 relating to modernisation and development of electricity public service, has deeply transformed the French electricity market. Today, France has adopted all the texts necessary to the transposition of the directive of 19 December 1996 on the electricity internal market². The market opening up has been chosen progressive and regulated. Public networks of transport and distribution will remain natural monopolies. The legislator has opted for the upholding of all these activities within the same integrated enterprise (EDF), with special mechanisms preventing abuses of a dominant positions and cross-subsidies. Access to networks is regulated by public authorities and transport fares as well. France held true to its commitments, although it has opted for the minimum percentage of opening provided for by the directive. This, however, represents 37% of the market.

Changing one's provider is now common practice for eligible customers.

For some, the French electric market seems locked; such an appreciation is excessive. On the one hand, interconnection capacities are sufficient to ensure supply for eligible customers located in other European countries. On the other hand, 50 competitors are active on the national territory, including two national enterprises which have become independent, CNR (Compagnie nationale du Rhône) and SNET.

In fact, the French electricity market is significantly open: by the end of 2002, about 17% of eligible customers (customers free to conclude supply contracts to cover their own needs with producers) had left EDF and chosen another provider. With leakages ("Joule effect") 25% of the open market is supplied with by other operators than EDF.

Moreover, after DGCCRF consultation, the legal person responsible for the unified management of the transmission system has called for a tendering procedure to buy the requisite generating capacity to offset a 11 TWh loss on the network.

The possibility of a partial withdrawal of the State from EDF's capital is no longer a taboo issue. The 100% State-owned enterprise is often criticized. It must be recalled that Community and national competition law are neutral as regards capital ownership. It is true, however, that public ownership entails suspicions about State aids and confusion concerning the role of the State as regulator and shareholder. In any case, one cannot enhance a single market if some enterprises limit access of foreign firms to a national market. In that respect, the traditional operator has not excessively resisted new entrants since only a few complaints have resulted in a CRE's decision relating to network access³.

The Act of 3 January 2003 creates a compensation system for public service charges. They are paid directly by consumers, but for non eligible customers (small professionals and households) the government has committed itself to lower tariffs by an equivalent amount.

² Directive 96/92/EC of the European Parliament and the Council of 19 December 1996 concerning common rules for the internal market in electricity. Official Journal L 027, 30/01/1997.

³ CRE, Decisions of 12 December 2002, "société PEMAR" and "société AESM", JORF 22 January 2003. CRE, Decision of 2 May 2002 "RATP", www.cre.fr/imgAdmin/1043236505531.pdf. CRE, Decision "société Dounor", 30 May 2002, www.cre.fr/imgAdmin/1024060527193.pdf.

Big customers' contributions are limited to € 500.000 whereas non-eligible customers' contributions are fixed at 7% of the 6 kVA tariff.

As for the **gas sector**, the Act of 3 January 2003 transposes the EC Directive of 22 June 1998⁴ which opens the gas market to competition for the most important customers (eligible customers). This provision is applicable until 2004, which is the date of the opening up of the market to all professional customers (households markets shall be concerned in July 2007).

In addition, a new tariffs formula, better linked with international energy rates variations has been introduced in 2001. DGCCRF has successfully advocated a mechanism according to which gas distributors shall pass half their annual productivity gains concerning commercial and networks costs on to consumers.

As to the percentage of eligible customers who have turned to another provider, France is relatively well placed, after the UK, Ireland and the Netherlands, and gas prices are, as well as those of electricity, under the European average.

2- The CRE (*Commission de régulation de l'énergie*)

The Electricity Act of 10 February 2000 has created a sectoral regulator, the **CRE** (*Commission de Régulation de l'Electricité*, recently transformed into the *Commission de Régulation de l'Energie*).

The existence of an independent body at this stage of the opening up process is based on various advocacy grounds:

On the one hand, highly technical issues require strong expertise,

On the other hand, the first phase is a transitional one, from a monopolistic market to a competitive market, this evolution needing regulation,

Lastly, because of the public status of the traditional operator (electricity and gas), the State would be both shareholder and regulator, if these functions were not separated.

The CRE is responsible for checking that unbundling rules do not allow discriminations, cross subsidies or competition distortions. DGCCRF refers to the CRE before fixing electricity and gas prices for purchasers who cannot choose a given provider. CRE also proposes networks access fares and settles disputes relating to networks' access (networks being essential facilities).

CRE's President refers anti competitive practices he may know in the energy sector to the Competition Council, if need be through an emergency procedure. CRE's President may also refer to the Competition Council any question relating to its competence. Reciprocally, the Competition Council may refer to the CRE any issue in the field of energy.

⁴ Directive 98/30/EC of the European Parliament and of the Council concerning common rules for the internal market in natural gas.

3- The application of competition rules

3-1 Anticompetitive practices

The Competition Council is competent at all stages of the opening up process for examining restrictive practices and, even before the operation of the abovementioned Directive of 1996, it imposed fines on several occasions.

In the field of the diversification of EDF-GDF's activities, the Competition Council fixed its doctrine in an opinion of May 1994.

Diversification of a traditional operator may imply competition distortions, such as predatory prices or cross-subsidies. The Council has stressed that the peculiar situation of traditional operators' subsidiaries permits them to obtain funds in a privileged manner, provides them with an easy access to final consumers thanks to a national network, and enables them to benefit from a service of general interest image. All these features represent assets.

The Competition Council advocated a series of steps to ensure that EDF subsidiaries operate like private enterprises of the same sector. It thus demanded the grouping of all diversified activities under a common holding that could have access to financial markets, subsidiarisation of each activity, as well as unbundling and legal autonomy for each subsidiary in order to check that diversification activities do not benefit, directly or indirectly, from monopoly's profits. The Council also mentioned the necessity to prevent EDF and GDF from certifying or requiring equipment or services produced by their subsidiaries.

On several occasions the Competition Council has sentenced EDF on the ground of abuse of its dominant position. For instance, the Council judged that the convention by which the city of Tourcoing granted to EDF street lighting maintenance for a ten years period at an artificially low rate constituted an abuse of a dominant position. The Council did the same analysis concerning street lighting maintenance contracts with 62 towns. The duration of the conventions was excessive (more than 5 years, renewable by tacit consent).

3-2 Merger control

In an opinion relating to the acquisition of Clemessy by EDF, Cogema and Siemens⁵, the Competition Council described the impact of the considered operation on competition. According to the principles set forth in its opinion of 10 May 1994, the Competition Council asked EDF to abstain from abuses of dominant positions when proposing global offers to eligible customers.

As far as non eligible customers are concerned, the Council noted that, given EDF monopoly concerning their electricity supply, every possibility of keeping on proposing technical or commercial services linked to electricity supply would *de facto* revive the possibility for EDF and its partners to propose a global offer to the same customers and would allow it to capture a part of the joint electricity sales provisions market. Such proposals would create artificial and discriminatory advantages vis-à-vis EDF's competitors, in particular when customers were on the verge of crossing the eligibility threshold.

⁵ Avis 2000-A-03 du Conseil de la Concurrence, du 22 février 2000, relatif à l'acquisition de la Société Clemessy par les groupes EDF, Cogema et Siemens (BOCCRF n° 10, 12 October 2000).

The Council also underlined the risk of disguised subsidies likely to emanate from purchase centralisation by EDF and Clemessy and from Clemessy's use of EDF-GDF Services centers' marketing power. In such a case, the advantages would not be offset by financial obligations reflecting real costs.

Last but not least, the Council warned EDF about placing the customer file at Clemessy's disposal because EDF was the only owner of this file concerning all the French consumers whether eligible or not. Moreover, from this file, EDF could know which enterprises were close to eligibility, whereas other electricity providers would be able to get the same information only when competent authorities have published the list of customers having access to the open market. The simple fact that Clemessy had direct access to this information would give it a substantial advantage to the detriment of its competitors on the electric installation market.

The Competition council finally considered that the merger was not anti competitive, provided its reservations were taken into account. The Minister of Economy and Finance cleared the operation on the condition that EDF and Clemessy accepted a series of undertakings following from the Competition Council's recommendations.⁶

In another merger case, the Ministry of Economy and Finance authorised:

- Vivendi Environnement's (through its subsidiary Dalkia) acquisition of EDF shares in the sector of related electricity production services in France and
- A joint control of EDF and Vivendi Environment on some EDF and Dalkia activities merged in three joint ventures (Dalkia Investment, Dalkia International and Dalkia Offre Globale).

In his letter of approval, the Minister of Finance reminded the principles contained in its previous decision (the Clemessy case). The Parties therefore committed themselves to a series of conditions similar to those prescribed in the Clemessy case, notably aimed at preventing any control of EDF on Dalkia activities on the downstream markets within the French territory. This explains why the Minister did not refer the operation to the Competition Council.⁷

⁶ Arrêté du 17 mars 2000, BOCCRF n°10 of 12 October 2000.

⁷ Lettre du ministre de l'économie, des finances et de l'industrie en date du 12 décembre 2000 aux conseils des sociétés Vivendi Environnement et EDF relative à une concentration dans le secteur des services liés à la production d'électricité. BOCCRF n°2, 23 February 2001.

4.3. THE JAPAN FAIR TRADE COMMISSION

APPROACH TO REGULATORY REFORM IN THE ELECTRICITY SECTOR

1. Approach to system reform

The Japan Fair Trade Commission (hereinafter “JFTC”) has studied how to establish an environment to promote competition in the electricity sector at the Study Group on Government Regulations and Competition Policy, which has already submitted a series of proposals. Most recently, in view of the direction of reforms of the electricity sector, the following have been studied:

- i) measures to encourage new entrants (implementation of efficient and fair connected lines, establishment of power trade exchange, etc.)
- ii) measures to activate wide-ranging competition (abolishment of the current transfer rate system)
- iii) establishment of fair rules in the consignment sector (separation of system administration from operations of electric power companies, etc.)
- iv) ensuring fair rules to promote competition in the electricity sector (establishment of a watchdog commission to ensure neutrality of system administration, etc.)

Based on the above studies, the basic approach toward establishing a competitive environment in the electricity sector has been formulated and the report, “Establishment of Environment to Promote Competition in the Electricity Sector” was released on June 28, 2002.

2. Amendment and publication of “Guidelines Concerning Appropriate Electric Power Dealings”

(1) Outline

To ensure that competition functions properly in the electricity market in conjunction with system reforms in 1999, particularly partial deregulation of electricity, the JFTC jointly with the (former) Ministry of International Trade and Industry drew up and published the “Guidelines Concerning Appropriate Electric Power Dealings” in December, 1999.

Subsequently because cases arose that had not been foreseen in the Guidelines, “Interpretation of the Antimonopoly Act Concerning the Partial Supply of Electricity” was drawn up and published in November, 2001 in order to prevent violations of the Antimonopoly Act.

Looking at these cases as well as the declarations, consultations, and so forth issued after partial deregulation, it was considered important to specify appropriate electric power dealings in greater detail to those concerned, including electric power companies, new entrants and users. Accordingly, the JFTC, jointly with the Ministry of Economy, Trade and Industry (hereinafter “METI”), amended and published the more substantial “Guidelines Concerning Appropriate Electric Power Dealings” on July 25, 2002.

(2) Main points of the amendments

Electric power companies have retained almost a 100 percent share of the electricity market in their respective service areas even after partial deregulation, and there has been almost no

competition among these companies. Where markets are dominated by regional monopolies, deregulated users or new entrants are forced to depend on the existing electric power companies for the supply of electricity as well as transmission lines, service lines, and so forth. It was therefore decided to specify in the Guidelines that, under such circumstances, setting disadvantageous conditions by electric power companies to new entrants or users wishing to start transactions with new entrants may hinder the business of new entrants.

Based on this standpoint as well as the cases examined and discussions with business operators, the following trade practices, for example, have been added to the Guidelines as possible violations of the Antimonopoly Act.

A. Retail supply and setting of retail rate to deregulated users

- . Setting and application by electric power companies of a disadvantageous tariff without proper justification to users who receive a partial supply, without offering the diverse choices normally made available by the companies.
- . Request by electric power companies of excessive prior notice in case of partial supply to users which follows the loading pattern

B. Wholesale to new entrants

Unilateral decision by electric power companies of items to be discussed with new entrants concerning backup support contracts in case of accidents.

Refusal by electric power companies to supply new entrants with that portion exceeding the extent of fluctuation (fluctuation of 3 percent or less of supply and demand) or setting of an unreasonably high rate

C. Consignment sector

Unreasonable postponement by electric power companies to new entrants of procedures prior to the commencement of consignment service

Restriction without proper justification by electric power companies to new entrants on the use of connection line equipment

D. New or additional construction of facilities by users who have power generation facilities for private use

Discounting by electric power companies of electricity rates, on condition that the users do not increase the power generation facilities for private use

3. A warning issued against Hokkaido Electric Power Co., Inc. and the implementation of the follow-up survey concerning “long-term contracts”

Hokkaido Electric Power Co., Inc. had concluded a “long-term contract” (in principle, 3 or 5 years) with users in the deregulated field, which included discounting the basic rate for the contract electricity guaranteed according to the length of contract, in which the company planned to charge an unreasonably high adjustment fee and penalty for cancellations due to switching the contract to new entrants, etc. The JFTC issued a warning to the company on June 28, 2002 as the practice may have been a violation of Article 3 of the Antimonopoly Act (Prohibition of Private Monopoly).

Subsequently, the JFTC conducted the follow-up survey concerning “long-term contracts” concluded with users in the deregulated field by other electric power companies and found that, in response to the warning issued against Hokkaido Electric Power Co., Inc., the companies had lowered the adjustment fee and penalty for cancellations which was to be charged due to switching the contract to new entrants, etc.

4. The statement of “the Viewpoint Concerning Regulatory Reform in the Electricity Sector”

The JFTC has been attending the meetings of the Subcommittee of the Basic Issues under the Electricity Industry Committee under the Advisory Committee for Natural Resources and Energy, the MITI. At the meeting of the Subcommittee, the JFTC made the statement on what should be considered from the viewpoint of the competition policy in securing the fairness and the transparency in the transmission departments, establishing a market for wholesale power exchange, eliminating the anti-competitive practices by the electric power companies, etc., on November 18, 2002.

5. Future approach

- (1) The JFTC, in order to establish an environment for fair competition in the electricity sector after the system reforms, will continue to actively address the matter based on the fundamental policy of system reform which was decided at the Electricity Industry Committee.
- (2) The JFTC believes that it is very important for the JFTC and the METI to collaborate and work together to promote further competition in the electric sector. Above all, the JFTC and the METI shall work in close connection with each other when administrating the new system, including the dispute settlements concerning the operation of the wholesale power exchange, the system administration, etc.
- (3) Further, the JFTC will continue to work to eliminate strictly and swiftly and prevent violations of the Antimonopoly Act and review jointly with the METI the current guidelines in accordance with the new system.

4.4. THE JAPAN FAIR TRADE COMMISSION

APPROACH TO REGULATORY REFORM IN THE GAS SECTOR

1. Approach to System Reform

The Japan Fair Trade Commission (hereinafter “JFTC”) has studied regulatory reform in the gas sector at the Study Group on Government Regulations and Competition Policy. This study group has already submitted a series of proposals and has recently studied deregulation and competition policy in the public service sector. Under the study group, a working group on the gas business was established. The working group has examined the evaluation of the system reform based on the amendment of the Gas Utility Industry Law in 1999 (expansion of the scope of partial deregulation for gas retail business), and has evaluated the future problems from the viewpoint of the promoting competition in the gas sector. The results of the examination were assembled in the report, “Problems with Competition Policy in the Gas Sector,” which was released on December 17, 1999.

The major points of the report are given below.

(1) Anti-competitive activities and preventing such activities in the gas sector

A further dose competition was introduced into the gas sector through regulatory reform in 1999. However, if an anti-competitive activity is conducted by businesses or business associations, the effectiveness of regulatory reform is impaired. Therefore, it is important that anti-competitive activities are clearly indicated. In addition, the JFTC, the government agencies in charge and gas companies will take actions to prevent anti-competitive activities.

Section 21 of the Antimonopoly Act, which is a confirmation clause, should be deleted.

(2) Future problems from the viewpoint of the competition policy

From the viewpoint of the competition policy, it is appreciated that, under the regulatory reform in 1999, the scope for large supply in the general gas business was increased, and consignment was institutionalized. However, the following items remain as future problems.

- A. Revision of the approval system for large supply
- B. Expansion of the scope of businesses to be covered by the notification and publication of consignment agreements
- C. Introduction of wholesale and consignment systems by new entrants in the wholesale and supply area
- D. Revision of uniform control over the general gas business
- E. Study on what the supply area of general gas companies should be
- F. Provision of information to users, such as consumers
- G. Promotion of competition in the gas business overall

2. Drawing Up and Publishing the “Guidelines Concerning Appropriate Gas Dealings”

After the amendment of the Gas Utility Industry Law in 1999, JFTC, jointly with the then Ministry of International Trade and Industry, prepared and published the “Guidelines Concerning

Appropriate Gas Dealings” in March 2000. The objective was to make the gas market function in a competitive manner. The guidelines indicate specific activities that are desirable from the viewpoint of fair and effective competition and activities that become problems under the Gas Utility Industry Law and the Antimonopoly Act. The guidelines cover the following areas: (1) The deregulated retail area, (2) the connection and supply area, (3) the wholesale area, and (4) the restrictive retail area. The guidelines cover cases that can become a specific problem in the gas market and expresses specific concerns.

3. Active Approach to Ensure Fair Competition in the Gas Sector

The JFTC attended meetings held by the Gas Policy Panel on December 13, 2002 as an observer. The meetings were held by the City Thermal Energy Sub-committee under the Advisory Committee for Natural Resources and Energy, the Ministry of Economy, Trade and Industry. The JFTC has made the statement on its basic ideas regarding securing free and fair competition in the gas sector.

(1) Basic ideas

The Gas Utility Industry Law should apply to the connection of pipelines and the non-deregulated segments, while the Antimonopoly Act should apply to the non-controlled areas and deregulated areas. As part of the system reform, the JFTC should thoroughly revise the “Guidelines Concerning Appropriate Gas Dealings” when adopting a new system to clarify which acts become problems under the Antimonopoly Act. In addition, the JFTC should strive for the strict enforcement of the Antimonopoly Act by improving its investigation system and establishing a consultation system.

(2) Ensuring fair competition for mutual entry of the electric power and gas sectors

It is important to promote the mutual entry of the electric power and gas sectors to promote free and fair competition in the both sectors. However, there is the concern that fair competition in one sector is impeded because monopolistic power is abused when entering into the other sector.

However, the imposition of restrictions on entry is not proper because it may lead to the protection of existing businesses. To secure fair competition for mutual entry, it is necessary to enforce divisional accounting and measures to isolate information under appropriate rules based on the respective business laws. It is proper that, thereafter, the JFTC will eliminate activities that may impede fair competition based on the Antimonopoly Act with the cooperation of government agencies in charge, and make an effort to prevent the said activities.

In addition, the JFTC will make it clear which activities are problematic under the Antimonopoly Act at the time of mutual entry in the “Guidelines Concerning Appropriate Electric Power Dealings” and the “Guidelines Concerning Appropriate Gas Dealings.”

4. Future Approach

- (1) The JFTC will continue to work actively after the system reform to create an environment of fair competition in the gas sector in consideration of the basic guidelines for system reform that were indicated at the meeting of the City Thermal Energy Sub-Committee.
- (2) In addition, the JFTC considers it important for the JFTC and the Ministry of Economy, Trade and Industry, the ministry in charge of the gas sector, to work in collaboration with each other from the viewpoint of promoting competition after the reform of the gas business

system. In particular, it is necessary for both organizations to collaborate closely concerning the rules on the connection of pipelines and the settlement of disputes.

- (3) Moreover, the JFTC will continue to pursue the prompt and quick elimination of activities violating the Antimonopoly Act to ensure free and fair competition in the gas sector, and revise the existing guidelines to accommodate the new systems. JFTC will conduct these activities in collaboration with the Ministry of Economy, Trade and Industry.

4.5. MEXICO: FEDERAL COMPETITION COMMISSION

ADVOCACY EFFORTS IN THE ENERGY SECTOR

1. Market structure and regulation

The advocacy activities by the FCC in the energy sector comprehends different industries with its own regulatory frameworks, these are electricity, natural and LP gas, the oil industry and its derivatives.

The oil and electricity industries are strategic areas reserved to the state according to the Mexican Constitution and are exempted from the monopoly provision of the competition law. The exemption does not include economic activities related with these strategic areas.

Strategic activities in the oil industry are extraction, transportation and distribution of hydrocarbides and some petrochemical products. These activities include the sale of first-handling of natural and LP gas and gasoline. Private firms can participate in the transmission, wholesale and retail distribution of natural and LP gas. Also, retail distribution of gasoline is currently franchised to private firms. The production of basic petrochemical products are reserved to state-owned Pemex. Other petrochemical products are supplied by state-owned Pemex and private firms.

Market structure of the oil and gas industry

Oil industry: Extraction, transport, distribution, first-sale

- State-owned firm

Basic petrochemical industry

- State-owned firm

Secondary and other petrochemical products

- State-owned firm
- Private firms

Transport and distribution of LP and Natural Gas

- State-owned firm
- Private firms

Retail distribution of LP and natural gas, gasoline and other fuels

- Private firms

The electricity supply is considered as a public service that comprehends generation, transmission, distribution and dispatch of power. The activities that are not considered as a public service can be developed by private firms which can generate or trade power for self-consumption, sales to electricity state-owned firms, exportation, importation for self-consumption and power generation for emergencies

There are currently two state-owned firms that offer public services in Mexico. One of them, the Federal Electricity Commission (FEC) is in charge of the provision of electric power that comprehends the planning of national electricity system as the generation, transmission and distribution of power. The FEC also purchases the power surplus generated by private firms.

The private firms can participate as independent producer, small-scale producer, and co-generation producer. This power generation is used for self-consumption, exportation and as mentioned before the power surplus could be sold to the state-owned FEC. The importation of power has to be authorized by Ministry of Energy and it has to be for self-consumption.

The independent generation of power is currently the way in which private firms participate in the electricity sector. The independent producer can generate power to export or to sell to the EFC through long-term contracts.

Market structure of the Electricity industry

Generation of power

- Two state-owned electricity firms
- Independent producers
- Co-generators
- Producers for self-consumption

Generation of nuclear power

- State-owned firm

Transmission, Distribution and dispatch

- Two state-owned firms

Competitive objectives in the energy sector

The FCC has set the following objectives in the energy sector:

- To promote competitive market structures in activities that are not reserved to the state.
- To prevent the state-owned firms, in charge of strategic areas, commit discriminatory practices related to its state-reserved activities.
- To support proposals for reform in markets currently to the state reserved, for example the proposal to reform the electricity sector.
- To increase faculties to the Regulatory Energy Commission and the setting of clear separation between faculties for regulation and competition. The current market situation in other regulated sectors denotes that market competition depends on the efficacy of regulation and on the co-operation between both competition and regulatory agencies.
- To advocate the application of competition principles in the design of laws, rules or legal orders. It is important to consider the efficiency effects of enacted laws, for example, the requirements for accessing or entering in the markets.

Entitlement of advocacy and coordination with other regulatory agencies

The FCC has three main activities of advocacy. Authorization for firms' participation in non strategic activities in the energy sector, effective competition statements in markets of LP and natural gas and emitting opinions on competition matters about regulations of the energy sector.

In the electricity sector, the FCC was consulted by the Federal Electricity Commission (FEC), the state-owned firm in charge of the national electricity system, about the desirability of evaluating independent producers' participation in the bidding of power-purchases made by the FEC. Currently, this market of power generation is closed to competition and independent producers have to sell its power to the FEC. The FCC, however, anticipated the sector reform and the fact that independent producers would be suppliers in the eventual creation of markets for power generation.

The FCC considered that the evaluation of bidders would be important to know the development and characteristics of new market structures and their eventual suppliers. The electricity market demands expertise of the technical design of electricity networks and to analyze the behavior of the power demand in national or regional markets. Although the electricity sector reform has not been implemented, the FCC's objective of evaluating firms in order to know the eventual markets that could be created is yet valid.

The FCC also evaluates the market conditions where economic agents ask permits for transmission, storage and distribution of natural and LP gas. Also, the natural and LP gas regulations empower the FCC to declare the absence of effective competition in order to set price regulations.

The following paragraphs introduced norms related to competition matters.

The LP Gas Regulation establishes the following:

“Article 7 Prices and tariffs

It is responsibility of the Ministry of Energy to set price and tariff regulations for the transport, storage, and distribution of LP gas.... when the assessment of non- existence of effective competition conditions is made by the Federal Competition Commission....

The Federal Competition Commission could declare ex-officio at any time the existence of competitive conditions or could do so by requirement of the Ministry of Energy, the Energy Agency, [the State-owned firm] Mexican Petroleum or by somebody affected” ¹

“Article 17 Economic competition

The [economic agents] interested in obtaining permits.. [for transport, storage and distribution], such as the possible holders of these permits ... [cession of permits], must notify their intention

¹ Artículo 7. Precios y Tarifas Aplicables.

Corresponde a la Secretaría, establecer la regulación de precios y tarifas aplicables al Transporte, Almacenamiento y Distribución de Gas LP., en el ámbito de sus atribuciones, cuando no existan condiciones de competencia efectiva, a juicio de la Comisión Federal de Competencia.

...

La Comisión Federal de Competencia, podrá declarar en todo momento la existencia de condiciones competitivas, ya sea de oficio o bien, a solicitud de la Secretaría, la Comisión, Petróleos Mexicanos o parte interesada.

to the Federal Competition Commission. This notification does not imply a merger notification”²

“Article 83 Information requirements

The Ministry [of Energy] or Agency [for energy] must give information to the Federal Competition Commission about the possible existence of cross-subsidies or other monopolistic practices notwithstanding their own faculties”³

The Natural Gas Regulation establishes:

“Article 12 Effective competition

When the Federal Competition Commission assesses the existence of effective competition, the general terms for the first-hand selling and the price of gas can be agreed freely ... if ... The Federal Competition Commission establishes that unduly discriminatory practices are committed the Commission [Regulatory] will reestablish the regulation of prices and the general terms and conditions of sale.”⁴

“Article 18 Information for economic competition effects

Those [economic agents] interested in obtaining permits [of transport, storage or distribution] must express their intention to the Federal Competition Commission and notify ... copy of application or its proposal ... for the effects of the Federal Law of Economic Competition”⁵.

Co-ordination with the regulatory agency and other authorities

The Federal Competition Commission and the Regulatory Energy Commission established an agreement in 2002 to coordinate their actions in areas of mutual interest, to exchange information and to exploit synergies between technical and economic knowledge in both

² Artículo 17. Competencia Económica.

Los interesados en obtener los permisos a que se refiere el artículo anterior, así como los posibles cesionarios de dichos permisos a que se refiere el artículo 25 de este Reglamento, deberán dar aviso de su intención a la Comisión Federal de Competencia. Este aviso no implica una notificación de concentración.

³ Artículo 83. Requerimientos de Información.

... La Secretaría o a la Comisión, en su caso, informarán a la Comisión Federal de Competencia sobre la posible existencia de subsidios cruzados u otras prácticas monopólicas, sin perjuicio de las facultades que correspondan a las mismas.

⁴ Artículo 12.- Competencia efectiva

Cuando a juicio de la Comisión Federal de Competencia existan condiciones de competencia efectiva, los términos y condiciones para las ventas de primera mano y el precio del gas podrán ser pactados libremente.

Si existiendo condiciones de competencia efectiva, la Comisión Federal de Competencia determina que al realizar las ventas de primera mano se acude a prácticas indebidamente discriminatorias, la Comisión restablecerá la regulación de precios y de los términos y condiciones a que dichas ventas deban sujetarse.

⁵ Artículo 18.- Trámite para efectos de competencia económica

Los interesados en obtener un permiso deberán manifestar su intención a la Comisión Federal de Competencia y presentarle, según sea el caso, copia de la solicitud de permiso o de la propuesta de licitación a que se refieren las secciones quinta y sexta de este capítulo, para los efectos de la Ley Federal de Competencia Económica.

agencies. The FCC hopes to overcome weakness of co-ordination currently observed with other regulatory agencies.

The FCC also participates in the Inter-ministerial Privatization Commission and in the Inter-ministerial Public Expenditure and Financing Commission. These Commissions set policies that involve state-owned firms such as in the energy sector. In these Commissions the FCC issues opinions about policies that affect both market efficiency and competition and seeks that regulatory provision prevents the abuse of dominant positions. The pricing policy for government goods and services, for example in oil products, is discussed in the financing commission.

The FCC's efforts over time

The FCC has supported the reform proposal for the electricity sector. The electricity reform has been under analysis since 1999. In that year the Mexican government submitted a reform proposal to the Mexican Congress that did not achieve sufficient political support. The FCC analysed eventual market structures for generation and distribution activities. In the year 2002 a new reform proposal was presented by the Mexican government which is currently under discussion. The FCC was required by some authorities to express its opinion about competition matters in the new reform proposal. The FCC has also presented its opinion in forums related to the electricity sector.

The FCC evaluates, since 2001, independent power producers to learn about the economic conditions in the eventual creation of markets for power generation.

The FCC has emitted opinions about the regulations of natural and LP gas sector.

The FCC stated in 2001 non effective competition conditions in 20 out of the 35 regional relevant markets of LP gas in the whole country. This was an important resolution since the LP gas is widely used by home consumers. Mexico is the world's highest home-consumer of LP gas. The Ministry of Economy applied a price's regulation in the whole country considering that LP gas is a basic product for home-consumers.

The FCC established in 1994 an agreement with Pemex, state-owned oil company, to reduce entry requirements for the installation of new gasoline stations. For example the minimum distance between gasoline station was eliminated as a requirement.

The FCC began an investigation in 1997 about an agreement between state-owned Pemex and one private firm for the exclusive distribution of lubricants in gasoline stations franchised by Pemex. As a consequence the FCC emitted in 2000 a resolution to prohibit the exclusive agreement investigated. Until 2003 Pemex announced that contracts of exclusive distribution were finished, but during this period the FCC promoted the benefits for consumer that would be achieved by introducing competition in this market.

In the petrochemical industry, the Mexican government has had the intention of privatizing the production of some petrochemical products not considered as strategic. The FCC has emitted opinions in different years about the desirability of privatizing these production units even though this policy has not achieved sufficient political support to be implemented.

5. Effectiveness of the FCC's contribution

The participation of the FCC has been effective for the analysis of economic agents that could participate in non state-reserved economic activities. This participation has permitted the FCC to evaluate the development of market structures. The evaluation of effective competition in LP gas markets also has conducted to price regulations in these markets.

The FCC has established a co-operation relationship with the Regulatory Energy Agency. The FCC hopes that this agreement decreases the transaction costs of coordination and implementation of both complementary competition and regulation policies. It will be relevant if the electricity reform makes progress. The FCC did not have, however, an important participation in the design of the electricity reform.

The energy sector is mainly considered as strategic sector by the Mexican Constitution. The advocacy activities of the FCC face political opposition that deters or delays the policy to promote market competition even in the non strategic activities, particularly when dominant firms, public or private, are involved. This fact was shown by the time it took to execute the statement of the FCC about exclusive distribution of lubricants.

4.6. SUBMISSION OF THE ANTIMONOPOLY OFFICE OF THE SLOVAK REPUBLIC

Advocacy in Energy Sector

The Antimonopoly Office of the Slovak Republic as a central state administrative body of the Slovak Republic (hereinafter AMO SR) with its exclusive force in the area of competition protection, enforces the competition policy as one of the components of state economic policy in order to develop a balanced competitive environment which in turn contributes to steady economic growth of the Slovak Republic.

Realizing this task the AMO SR reached the biggest success right in the electricity industry, which it had been focused on already after the establishment of the AMO SR in 1990. In that period the Slovak electricity sector was fully vertically integrated in the production, high-voltage transmission and in distribution. Right through the distinct application of competition advocacy the AMO SR even at the beginning of its activity succeeded in convincing the Ministry of Economy to separate 3 distribution enterprises from the organizational structure of the Slovak electricity sector. Thus three independent distributors have been established according to the territorial country division and the full vertical integration has been disturbed for the first time.

The AMO SR realized that it was necessary to go ahead intensively in establishing competition principles in this industry, not only by the realization of structural changes, but also by the parallel gradual changes in the area of regulation framework. The Ministry of Economy, as the sectoral ministry, directly responsible for the energy area did not realize and even was not interested in realizing any steps in this direction, the AMO SR introduced in 1992 the draft of the Act on natural monopolies regulation, which assumed all the regulation forces to be transferred to one body. In that time most of the central state administrative bodies did not agree with the creation of a regulatory office relatively independent from the government, so the mentioned legislative initiation of AMO SR has been stopped. The political will to transfer regulation forces from the Ministries of Finance and Economy to the regulatory body, independent from the government has been missing, so this activity failed also from the reason that the legislative surroundings were not ready for the creation of such an act.

In 1994 the AMO SR repeatedly submitted a draft of the **Act on natural monopolies regulation**. Its aim was to abolish existing imperfections and to create unified legal, economic and organizational presumptions to regulate natural monopolies (generation, transmission and distribution of electricity, heat, gas and water). At the same time AMO SR was approaching the intention to create presumptions for the simulation of a competitive environment, for the support of the natural initiatives of entrepreneurs towards increasing efficiency and higher quality of supplies to the benefit of consumers. AMO SR considered the adoption of this standard as one of the basic presumptions for the successful privatization and a part of restructuralization in these areas of business.

Then a several years-long effort of AMO SR followed with the aim to persuade relevant ministries (it means Ministry of Finance and Ministry of Economy, which shared the responsibilities in the area of regulation) and also persons managing the energy sector itself, that it is necessary to start introducing changes in the energy industry, which should gradually lead to the creation of conditions to develop the competition in this area as well. This effort was realized

through the participation of determined AMO employees in various events connecting with the energy industry, like conferences, speeches, seminars, participation in various working groups and also through the enforcement of competition principles directly by the Chairman of AMO SR, who did and still does participate in the sessions of advisory bodies of the Government, even the session of Government of the Slovak Republic itself.

However after all, following the parliament elections in 1998 the newly created government assigned in its Policy Statement as one of its aims to legislatively prepare and to institutionally realize the more effective regulation of natural monopolies in energy sector and in other network industries and to create the common institution executing the state regulation of making business in the network industries. At the same time the government named the working group for the creation of legislative framework and for the regulatory body establishing. Also the representative of AMO SR has been nominated to this working group.

Draft of the act has been prepared in August 2000 and after the inter-ministerial comment proceedings, where AMO SR played the significant role the draft has been submitted to the governmental advisory committees for its assessment. In February 2001 it was submitted to the session of the Government of the Slovak Republic. During the negotiations on the act in the governmental committees its content went through certain changes also based on the requirements of AMO SR. Act on Regulation of Network Industries came into force on August 1, 2001 and the regulatory office is now responsible also for the area of regulation of drinking water supply and the regulation of used water disposal.

The Office for the Regulation of Network Industries has been established in 2001 and its role is the state regulation in the network industries. Network industries are generation, purchase, transmission and distribution of electricity, gas, heat, production and supply of drinking water and disposal and treatment of sewage.

AMO SR significantly urged to come out from the same principles and to follow the same targets in constituting of regulatory body and also in the creation of connecting legislation as are used in the creation of similar standards in the countries with the developed market economy.

In spite of the achieved significant progress, as in the case of telecommunication regulator, AMO SR is still interested in cooperation in certain details improving, for example that the regulatory office ought to be independent in the terms of its financing as well.

The AMO SR achieved another success in realization of competition advocacy in electricity industry recently, when it succeeded in enforcing the idea of separation of high-voltage transmission grid, after almost 10 years of permanent emphasizing of the necessity of such a step in the governmental sessions, sessions of governmental advisory bodies, in the standpoints to the various materials regarding the energy sector. Finally in 2001 the material dealing with the separation of transmission system, restructuralization and privatization of *Slovenské elektrárne* (Slovak Electricity Works) has been submitted to the session of the Government of the Slovak Republic. Subsequently the separation of high-voltage grid has been realized last year, so the vertical integration became history. Thus through the advocacy the AMO SR actively asserted the idea to separate generation, transmission and distribution of electricity. Distribution enterprises successfully undergone the privatization and today the first steps to privatize the generation, it means the privatization of *Slovenské elektrárne*, are being realized.

We can positively say that the steps order in electricity sector is furthermore realized under the certain cooperation with AMO SR, as effectual authority in enforcement of basic principles in creation of competition surroundings to the electricity industry therefore today aiming to maintain these principles also after the completing of the privatization process. Anyway AMO SR noticed certain efforts to return the vertical integration back and the certain danger that the effort of the AMO SR might be harmed is still alive.

One of the real activities of the AMO SR regards already started privatization process of the incumbent producer of the electricity it means *Slovenské elektrárne*. The AMO SR addressed Minister of Economy in this matter with the intention to warn him about the fact that during the privatization the unfavorable interconnection of the structures of ownership may occur, which should eliminate the existing effort of AMO SR to develop the competition surroundings in this area.

The subjected issue, which the AMO SR has already warn about since the submission of first drafts on privatization of *Slovenské elektrárne* comes from the fact, that these drafts comprise also the alternatives, selections and realization of intentions which should be assessed by the AMO SR pursuant to the Act as non-acceptable from the view of competition protection. It is necessary to emphasize that in the subjected matter the issue refers to the companies, which would, in case of their success in tender, strengthen their dominant position on the relevant market of electricity supplies due to their acquired control over the distribution companies. This situation would result in creation of obstacles to the effective competition.

AMO SR permanently emphasizes in all forums that several legislative steps have been accepted recently, which create the presumptions to liberalize energy sector in the Slovak Republic in harmony with the legislation of European Union. But the AMO SR considers these steps as *conditio sine qua non* of the energy sector liberalization, but not sufficient to create market and competitive conditions in energy sector. The connection of company producing electricity, *it means the industry segment where the presumptions to develop competition among individual market participants exist* with the company providing the electricity distribution, *it means the industry segment with no possibility to establish the competition*, is assessed by the AMO SR as a fact not contributing to the competition development, but vice-versa as a fact directly creating presumptions to obstruct the process of energy sector liberalization and it is also likely to make the level and conditions of liberalization worse than they are today.

The standpoints of the AMO SR are also based on the recommendation presented by the representative of the International Energy Agency at the international conference Energy Effectively in November 2002 in Prague, when he in his speech stated that the privatization ought to be used to strengthen, not to weaken the separation of network services, production and retail supplies. At the same time he recommended for the electricity sector to ensure to have transmission and distribution companies as the independent subjects separated from the competition business of energy production and supplies.

4.7. SWISS SUBMISSION ON THE ELECTRICITY SECTOR

A. INDUSTRY BACKGROUND, STRUCTURE AND PLAYERS

1. The Swiss electricity sector is extremely decentralized by European standards. It has 1200 active companies in the sector alone including 200 who are exclusively involved in generation. In addition, 300 companies are vertically integrated and span at least two of the generation, transmission and distribution sectors. Within these 300 companies, seven are vertically integrated companies. Thirty companies are engaged in international trade while the remaining 700 companies are mainly involved in local distribution.

2. Five integrated companies dominate the Swiss market, holding a share of approximately 80% of the wholesale market. These five companies have formed an industry association called 'Swisselectric' to promote common interests. These companies typically cover a demarcated distribution area with direct sales or with indirect sales through partners or – as for Axpo and EOS – their shareholders. They have their own production capacities, but often jointly own large hydropower or nuclear plants. Furthermore, several companies have drawing rights on French nuclear plants. Due to their stakes in disseminated large production capacities, company-owned grids are sometimes far-flung, jointly owned and intermeshed.

3. There are approximately 2300 electricity generation plants, the 25 largest of which account for almost 60% of power generation. At the other end of the spectrum, 800 micro-hydro plants, 450 combined heat and power plants, and 600 photovoltaic and wind power installations contribute just over 1% of electricity generation.

4. 75 % of the total electricity sector capitalization is publicly owned (federal state, cantons, municipalities), and 12% of capitalization is foreign-owned.

5. In contrary to some expectations, the sector has not undergone sweeping ownership changes in recent years. In particular, no major privatization has occurred, as several plans for 'Corporatisation' of public (mainly municipally)-owned utilities have been thwarted by popular votes. Nevertheless, there were some important ownership changes: Some large European groups purchased stakes in Swiss utilities including the publicly owned Axpo/NOK which bought out both of E.ON's and EnBW's 24.5% shares in Watt in 2002.

6. Most large electricity companies, with the notable exception of EOS, display healthy balance sheets in spite of major price discounts given to large customers. The large electricity companies reported efficiency gains over the past few years, which enabled them to lower their average hydro production costs to "close to European levels". But companies concede that further cost cuts are needed – mostly through more automation – to become fully competitive at the international level. Part of the streamlining, however, is achieved through tax cuts, particularly with respect to the water use royalty levied by the cantons.

7. Some large Swiss companies geared up for European market liberalization by creating (joint) purchasing/trading companies and setting up subsidiaries abroad. A group of large municipal utilities formed 'Swisspower' to pool their marketing services.

8. To sum up, the Swiss electricity market is fragmented into a large number of publicly owned regional or local monopolies. Cantonal and local governments intervene through

regulation and taxation, and often earnings from their utilities provide a sizeable share of their budget revenues. The wide price dispersion across monopoly regions suggests large hidden costs.

9. On the consumer side, there are 130 large corporate consumers (using more than 20 GWh/year) who account for 30% of consumption.

10. Future changes in the Swiss corporate landscape are difficult to predict, particularly after the defeat of the Electricity Market Law (EML, see below). Widespread mergers and acquisitions of local utilities, as feared by some if the EML went through, are unlikely to happen in the near term, since local monopolies received a political plebiscite through the EML vote. Some, however, may spin off their marketing/trading functions to more seasoned larger companies. Similarly, there is no reason to foresee massive foreign acquisitions of large Swiss companies, given their robust balance sheets and often-sizeable public ownership structure.

B. Competitive objectives and legislative/regulatory change designed to further these objectives

11. The opening of the Swiss electricity market has been a growing concern in Switzerland since the liberalization in the European Union market. Fair and efficient competition in the Swiss market has been considered an objective to prevent the Swiss economy from suffering a competitive disadvantage from foreign competitors.

12. The main competitive objective is to liberalize the power generation market. This requires, on the one hand, that all power-generating companies have non-discriminatory access to the transmission and distribution network, and on the other hand, that users can freely choose their power supplier.

13. To achieve these competitive objectives, the Swiss Parliament adopted the Electricity Market Law (EML) in December 2000. This new legislation was designed to liberalize the Swiss electricity market through a six-year transition phase. In Switzerland, a new law enters into force only after the expiration of a three-month period during which time a referendum can be taken regarding the new law. The trade unions, later rallied by a coalition of various leftist and vested municipals interests, launched a referendum, in Spring 2001, against the decision of the Parliament. The referendum was positioned as a battle against deregulation proper. In an unusual step, the Government chose to elaborate an implementing ordinance to the EML ahead of the referendum, so as to lay down the technicalities of the planned electricity market liberalization.

14. By means of a national vote, the Swiss population was asked on September 22nd 2002 if it backed the liberalization process proposed by the legislative body. The EML was rejected by the Swiss electorate by a low margin of 52.6 % of the voters. The reasons for this defeat are complex and manifold. Whereas the benefits for the industry were obvious, the domestic consumers did not see the urgency and utility of the new legislation.

15. The main features of the EML were:

- Unbundling (at the accounting level) of generation, transmission and distribution.
- The creation of a newly created company to administer the transmission network. Regulated third-party access and non-discriminatory and transparent transmissions tariffs. A Federal Arbitration Commission would be set up to address disputes pertaining to

distribution and transmissions tariffs. However, this Arbitration Commission shall consult, in the event of tariff disputes, the Office of the Price Supervisor and must based its decision on this authority's opinion.

- Gradual opening (up to 6 years) of the market to eligible consumers (first to large consumers i.e. more than 20 GWh/year)

C. Source of authority to engage in advocacy

16. The Swiss Federal Act on Cartels and Other Restraints of Competition (Act on Cartels; Acart) as of October 6th 1995 provides two advocacy provisions:

Art. 45 §2 Acart:

“The Commission may address recommendations to the authorities, the purpose of such recommendation being to promote effective competition, especially with regard to the drafting and enforcement of laws relating to economic affairs”.

Art. 46 Acart:

1. The secretariat shall review draft confederation legislation, especially in economic matters, that is likely to influence competition. It shall determine whether the effect of such legislation is not to introduce distortions or excessive restraints on competition.
2. In the consultation procedure, the Commission shall adopt a position with regard to the draft confederation legislation that limits or influences competitions in anyway whatsoever. It may issue opinions on draft cantonal legislation.”

D. The agency's efforts over time

17. The Federal Competition Commission (hereinafter: Comco) and its Secretariat have been dealing for several years with the liberalization process occurring in the Swiss electricity market. During the drafting procedure of the Electricity market Law (EML), the Secretariat has been able to bring in important competition policy considerations. Formally, the Comco has issued two opinions in the frame of Art. 46 §2 Acart: the first on the draft of the EML itself and the second on its related ordinance (RPW 1998/2, p. 320 and RPW 2001/4, p.787).

18. Throughout the consultation procedure, the Comco strongly supported a rapid and broad liberalization of the electricity market. The Comco spoke against the bill's provisions for compensation of sunk costs of power-supply companies, since they were able for decades to burden all the costs on consumers and to profit from considerable monopoly rents. Because the transmission network constitutes a natural monopoly, the Comco supported the draft's proposition to create a national company to operate the national power grid.

19. Since the adoption of the EML failed in September 2002, no regulatory changes have taken place in Switzerland. Nevertheless, the Swiss competition authorities continue their efforts to promote competition in the electricity sector through competitive enforcement actions. According to the newly appointed the Comco's chairman Walter A. Stoffel, the opening of the electricity market will be one of the highest priorities of his

mandate. Though the competition authorities are fully aware that isolated decisions in particular cases cannot replace a broad market opening as foreseen by the EML, they are determined to use all the means available to eliminate severe abuses.

20. For example the Comco argues that the distribution network constitutes an essential facility and that refusal to transmit against payment may violate the Act on Cartels. The Comco closed a case in February 2000 where the BKW Energy Corporation (BKW) refused to transmit third party electricity for one of its former customers. Finally, BKW offered to the mentioned customer a more favorable contract than the competitor involved in the case. Perhaps the most important case that the Comco has had to deal with was the “EEF case” involving Migros (the largest Swiss retailer and supermarket chain) and its power supplier Watt and EEF, (the electricity utility of the canton of Fribourg). Watt and Migros had agreed on a contract for electricity transmission to two local branches of Migros situated on the monopoly area of EEF. EEF refused to afford Watt transit through its grid. The Comco ruled in favor of Migros/Watt stating that EEF’s refusal to give access to its grid constituted an abuse of dominant position, which contradicts the Swiss Act on Cartels. The Appeals Commission for Competition (hereinafter: REKO) Matters confirmed the ruling shortly before the failure of the EML. The REKO did not bear the plaintiff’s argument that the electricity market was a publicly regulated market and therefore exempted from the Act on Cartels. So far, an Appeal has been lodged by EEF before the Federal Supreme Court in Lausanne.

21. Several other investigations were opened in the electricity sector, all of which are now shelved awaiting further clarification after the demise of the EML. Of interest as well is an investigation launched in March 2002 about contracts by four electricity companies of Axpo. The contracts were designed to lock established resellers into long-term commitments so as to prevent them from changing their suppliers in case the market opens. Such contracts to bar new market entrants could be considered an abuse of dominant position according to the Swiss doctrine of competition law.

E. Agency’s contribution

22. The intervention of the Swiss Competition Authorities in the drafting procedure of the EML through opinions is difficult to assess since the EML failed. The enforcement actions of the Commission could contribute to opening the market and have a deterrent effect upon dominant enterprises. For instance, an electricity company that refuses transmission must expect that the Comco opens an investigation. Partly as a consequence of this, many large electricity consumers have succeeded in negotiating price economies of up to 30 percent with their current supplier.

23. However, the effectiveness of the intervention of the Comco in the future will largely depend on the outcome of the EEF’s appeal before the Federal Supreme Court. The Supreme Court may not take into account non-specified public interests, such as public service. If the Supreme Court holds that the Act on Cartels is not applicable to the electricity sector, the scope for maneuver of the competition authorities will be reduced. Finally, there is also the possibility of an exceptional authorization by the Federal council on the grounds of compelling public interests. Some political commentators believe that the Federal council may find it politically arduous to uphold the Comco’s ruling, given that the “public” clearly voiced its view in the referendum.

24. That being said, the effectiveness of the agency contribution, though notable, is limited since particular case decisions cannot enforce a general Third Party Access obligation, nor do they set up general rules regulating transmission reimbursement. The above-mentioned decisions, if upheld, have set important precedents but could not be automatically applied to other cases. Therefore, if large producers or consumers want to “elbow” access through another operator’s grid with the help from the Comco, they would need to file on a case-by-case basis– a long and costly endeavor.

25. In addition to the uncertainty of the extent of the applicability of the Act on Cartels to the electricity sector, other issues are looming ahead like the reactions of the European Union (transit) and of the European trading partners (reciprocity) to the refusal of Switzerland to open its market. Market players and observers pin some hope on voluntary agreements by the industry – similar to the German “Verbändevereinbarung” - whereby the main integrated companies would agree to negotiate Third-Party-Access. By Spring 2003, the Federal council and the Swiss Federal Office of Energy have decided on the basis of consultations with various interested groups that three areas need something to be done:

- First, the international position of the Swiss electricity market has to be secured.
- Secondly, the electricity prices have to be lower down.
- Thirdly, power supply must also be ensured in the liberalized area.

4.8. UNITED STATES DEPARTMENT OF JUSTICE

SUBMISSION ON ENERGY TO THE ICN COMPETITION ADVOCACY SUBGROUP

INTRODUCTION

This paper is a reference of practical experience for countries seeking to implement a competition advocacy program regarding their energy industries. An obvious first step in competition protection advocacy is to develop a reasonable understanding of how the industry operates and the economic issues that have been raised in policy discussions about the industry domestically and abroad.¹ Understanding of the industry's economics, institutions and history is essential as it makes it much easier to understand the more detailed aspects of the industry and how the positions of various firms and other organizations relate to their respective interests. Such background information also enables a competition agency to develop more effective lines of inquiry in interacting with industry participants. Without such a general understanding, it is easy to miss the significance of events and new developments and it is easy to fail to be taken seriously in discussions with regulators and other policy makers.

There are several commonsense ways to gain an understanding of major issues in an industry. A prudent initial step is for the competition agency to work with economic experts in the industry to supplement information gleaned from the industry trade press or from other research done by the agency. Informal communications with local university professors can be extremely helpful. There are several advantages to working with an expert. First, an economic expert typically already has a general understanding of industry competition issues. Working with such an expert is a very efficient way for agency staff to acquire such an understanding of the industry themselves. Second, the expert usually has a network of personal contacts and is aware of industry data sources. This can make agency efforts to document industry facts, trends, and peculiarities much more efficient. Third, the expert usually has developed a good understanding about which parties are the strongest advocates for different policy positions. This can help the agency understand the main positions before the agency develops its own position; it also can help the agency evaluate conflicting claims of interested parties more effectively. Fourth, the expert can give agency staff confidence that it understands the issues. This comes from repeatedly asking the expert if his or her understanding corresponds to the staff's understanding. Fifth, the expert can provide a standard for determining when the agency has developed a reasonable initial understanding of the industry. This test is satisfied when staff can carry on an extended discussion of the industry with the expert without learning much that is new.

Another useful way to obtain background information may be to network with former staff of the competition agency who have left the agency to work on industry issues. Informal contacts with former staff may help in the early stages of understanding the industry and its issues because a former staff member typically understands and appreciates the perspective that the agency brings to its advocacy efforts. Networking with individual interest groups may be another viable way to gather background information about an industry such as the electric power industry.

¹ This introduction is taken from John Hilke, *Joining the Electric Industry Policy Debate at the State Level*, in *THE ANTICOMPETITIVE IMPACT OF REGULATION* 378-393 (Giuliano Amato & Laraine Laudati, eds., 2001).

I. COMPETITION ADVOCACY IN THE UNITED STATES

The United States has two competition enforcement agencies: the Antitrust Division of the United States Department of Justice and the Federal Trade Commission. The Department of Justice is part of the executive branch of government; the Federal Trade Commission is an independent agency. Each agency enforces the antitrust statutes and each also has an active competition advocacy program. This section discusses the activities of both agencies. It begins by discussing the structure of the energy industries in the United States. It then gives examples of advocacy methods (regulatory interventions, reports, networking with agencies, *etc.*). This section is not a comprehensive catalogue of competition advocacy activity of the agencies, but rather, a set of case studies. The section ends with a note on the criteria for assessing the success of competition advocacy programs.²

A. Structure of the United States' Energy Industries

In the United States, the energy industries historically have been largely composed of private enterprises subject to regulation by the federal, state and local governments.³ This section will discuss separately the electric utility industry and the natural gas and the oil pipeline transportation industries.

1. Electric Utility Industry

The electric utility industry developed primarily as a collection of private investor-owned utilities that historically owned the distribution wires connecting their generation sources to local load. As the owner of the distribution wires and generation sources, these vertically-integrated companies provided a bundled (delivered power) product to consumers, both firms and individuals. Until ten years ago, vertical integration was the norm for electric utilities in the United States.

Because generation and distribution were local, the states were the first governmental bodies to regulate these vertically-integrated companies.⁴ In addition to regulating rates, the states also regulated entry, issuing exclusive rights to sell and distribute electricity to end-users (*i.e.*, to provide retail electric service) in defined geographic areas. As the industry continued to evolve, however, individual states found it more difficult to regulate the multistate operations in these industries.

²This section is a joint effort by staff of the two US antitrust enforcement agencies: the Department of Justice Antitrust Division and the Federal Trade Commission. Much of the following is taken from three papers: Jade A. Eaton, *Recent United State Department of Justice Actions in the Electric Utility*, 9 CONNECTICUT JOURNAL OF INT'L LAW 857 (1994); Jade A. Eaton, *The Dance of Regulation and Competition: Regulation and Deregulation of the Natural Gas Industry*, Prepared for OECD/World Bank Conference on Competition and Regulation in Network Infrastructure Industries (June 1994) <[http://www.oilis.oecd.org/olis/1995doc.nsf/224cf01435f3f28580256564005f9d8a/1cd237f45171825cc12562130031d776/\\$FILE/CLE5205.ENG](http://www.oilis.oecd.org/olis/1995doc.nsf/224cf01435f3f28580256564005f9d8a/1cd237f45171825cc12562130031d776/$FILE/CLE5205.ENG)>; Hilke, *supra* note 1.

³ Although there are some large energy projects government owned and operated, these are primarily major hydroelectric projects involving dams on navigable rivers.

⁴ Since 1920, hydroelectric projects on navigable rivers have been subject to federal licensing requirements. Federal Power Act of 1920, 41 Stat. 1063.

In the 1940s, transmission networks became interconnected and began to cross state borders. As a result, no one state had jurisdiction to effectively regulate the ownership or operation of electric (or gas) utilities. In response, Congress passed the Federal Power Act and the Natural Gas Act. These acts allowed the federal government to regulate aspects of the industries affecting interstate commerce. The Federal Power Act requires the Federal Energy Regulatory Commission to review rates paid for electricity sold at wholesale, that is, electricity sold not to the ultimate consumer but to an entity that intends to resell the power to a consumer. Sales to consumers, which are largely made by for-profit firms, remain subject to regulation by state authorities.⁵

2. Natural Gas Industry

In the United States, the natural gas industry consists of private for-profit firms that are involved in all aspects of the industry, including exploration and development, gathering and processing, and transportation and distribution. There are pipeline companies that gather gas in the field and process it so that it can be transported via interstate pipelines. In addition to such long-distance transporters, there are local distribution companies that distribute and sell gas to individual businesses for use in industrial and commercial processes, and to households for use in cooking and heating.

The natural gas industry in the United States is subject to regulation by the state and federal governments. At some point in time there has been federal regulation of entities performing almost every function in the natural gas industry. At present, however, price and allocation of natural gas sales at the production and wholesale levels are completely unregulated. States traditionally have regulated some aspects of natural gas production and have also regulated the companies that distribute natural gas to retail customers.

3. Petroleum Industry

In the United States, there are companies involved in all segments of the petroleum industry. Domestically-produced crude oil is carried from the field in gathering pipelines to rail heads, barge terminals on large river systems and larger diameter long distance transmission pipelines. Tankers deliver imported crude oil to deep water ports and other terminal facilities. The crude oil, domestic and imported, is delivered to refinery centers where petroleum products are produced. These products are distributed by rail, truck, barge, tankers and large diameter long distance petroleum pipelines to regional tank storage facilities. From these storage facilities, petroleum is loaded onto tank trucks which deliver to retail distribution points such as gasoline stations or, in the case of heating oil, to homes and businesses.

The industry consists of private for-profit firms⁶ subject to little regulation at the local or national level. Production of crude oil is sometimes subject to state “rate of take” regulation that is aimed

⁵ Private, for-profit firms account for 75 percent of retail sales; cooperatives, municipal systems and state and federal power authorities account for the remaining 25 percent. An overview of U. S. electric power industry is available from the Energy Information Administration of the U.S. Department of Energy. See <<http://www.eia.doe.gov>>.

⁶ As a result of The Energy Policy and Conservation Act of 1975, Pub. L. No. 94-163, 89 Stat. 871 (1975), however, the federal government owns substantial petroleum stocks maintained in the Strategic Petroleum Reserve.

at conserving natural resources from common production formations.⁷ With the exception of World War II and later briefly in the wake of the oil embargo, the federal government has not engaged in price and allocation regulation of crude oil and petroleum.⁸

B. Goals of Legislative/Regulatory Change in the United States

Unregulated firms in the United States are subject to the antitrust laws. Moreover, regulated firms may be subject to the federal antitrust laws: enforcement of federal antitrust laws and federal regulation of industries are not assumed to be mutually exclusive. For example, over twenty years ago the Antitrust Division sued to enjoin a regulated vertically integrated electric company from refusing to sell wholesale power or transmit another's wholesale power to a competitor's retail customer.⁹

As noted, two agencies are charged by statute with enforcing the antitrust laws in the United States: the Antitrust Division and the Federal Trade Commission or FTC. In addition to the enforcing the antitrust laws, the Antitrust Division and the FTC are authorized by statute to engage in competition advocacy before regulatory agencies.¹⁰

The Antitrust Division recognizes that regulation has a role to play where market failure or other externalities interfere with the efficient allocation of goods or services.¹¹ The Division also recognizes that regulation can increase inflexibility and administrative costs and should not be imposed where it is not necessary. Issues of competition and regulation are especially prominent in industries that have recently undergone regulatory change like the electric industry.

Through its program of competition advocacy, the Division seeks to further four goals:

1. Eliminate unnecessary and costly existing regulation;
2. Inhibit the growth of unnecessary new regulation;

⁷ See, e.g., OKLA. STAT. tit. 52, § 240 (2002).

⁸ Emergency Petroleum Allocation Act of 1973 (EPAA), Pub. L. No. 93-159, 87 Stat. 627 (1973) (repealed 1981). Because of a perception of disparate bargaining power (rather than any natural monopoly problems), there is law regulating the relationship between refiners and their branded retail outlet franchisees. See Petroleum Marketing Practices Act (PMPA), 15 U.S.C. § 2801 *et seq.* (2002).

⁹ See *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973).

¹⁰ See 28 C.F.R. § 0.40(b) and (g) (1993) (authorizing competition advocacy by the Antitrust Division). Statutory authority for FTC advocacy efforts is provided in Federal Trade Commission Act, § 6 (authorizing the FTC to prepare reports and publicize findings). Authority for the FTC to engage in competition advocacy traces back to the origins of the FTC. The FTC was originally envisioned as an agency to investigate and publicize studies about competition issues. During the first half of the 20th century, when neither Congress nor the Office of the President had substantial investigative staffs, the agency undertook many such studies at the request of Congress or the President. Although the FTC is now predominantly a law enforcement agency, its competition advocacy role remains active. In addition to the statutory authority to promote competition, budgetary authority for competition advocacy by the FTC takes place during each budget cycle through Congressional oversight of the FTC's budget appropriations.

¹¹ This discussion of the Antitrust Division's advocacy program is taken from U.S. DEPT OF JUSTICE, ANTITRUST DIV. MANUAL ch. V (3d ed. 1998) <<http://www.usdoj.gov/atr/foia/divisionmanual/five.htm>>.

3. Minimize the competitive distortions caused where regulation is necessary by advocating the least anticompetitive form of regulation consistent with the valid regulatory objectives; and
4. Ensure that regulation is properly designed to accomplish legitimate regulatory objectives.

In analyzing the need for new or continued regulation, the Division attempts to focus attention on the comparative benefits of free competition, on the one hand, and the proposed method of regulation, on the other, by asking several basic questions:

1. What are the costs or disadvantages of free competition in the market or industry at issue?
2. If the regulatory scheme is an existing one, has regulation fulfilled its purpose; and, do the underlying economic and social conditions justifying regulatory interference with the marketplace still exist?
3. What are the costs and benefits associated with the existing or proposed regulatory scheme?
4. If existing regulation is to be eliminated, what are the necessary elements of a transition from regulated to a competitive, unregulated market?
5. If regulation is appropriate, is the particular regulatory scheme well-tailored to achieve its purpose?

Asking these questions requires that those who favor regulation demonstrate that the benefits to the public of regulation outweigh its anticompetitive effects; that such benefits cannot be achieved by some less anticompetitive alternative; and that, where regulation is needed, it be wisely crafted to accomplish its objectives with no unintended consequences. Where these showings cannot be made, the case for regulatory reform, up to and possibly including the elimination of regulation, is likely to be compelling.

The Division's Transportation, Energy and Agriculture Section has responsibility within the Division for a number of regulated industries, including the regulated energy industries. Among the Section's competition advocacy activities is the submission of comments to the Federal Energy Regulatory Commission (FERC). In general, in its comments to regulatory commissions, the Division argues that wherever possible, the agency should adopt policies that rely on market mechanisms instead of legal mandate. Because unregulated markets depend on free and unrestricted competition to set prices and output at efficient levels, compliance with antitrust laws is crucial to the success of deregulation and regulatory reform. Markets where competition is sufficient to allow market-based pricing, for example, are precisely those markets where antitrust compliance and enforcement are urgently needed. Thus, the Division's advocacy of market mechanisms in what were strictly regulated industries is accompanied by a renewed commitment to antitrust enforcement in those newly competitive markets.

C. Competition Advocacy Case Studies

The Antitrust Division and the FTC engage in competition advocacy in many ways. For example, the agencies provide advice on legislation, they comment on rulemaking proceedings at regulatory agencies, they intervene in the regulatory administrative proceedings regarding

specific parties or transactions, and they seek to influence policy through informal contacts with policy makers and industry participants. This section provides brief case studies of these competition advocacy methods.

1. Advising Legislatures: The Petroleum Industry

Competition advocates can use reports to and correspondence with legislators to provide advice on regulatory policy. Although legislators can choose to ignore such advice, the information provided in reports or correspondence often can provide factual or theoretical justification for policies that may be difficult to maintain politically. This approach can be used even in circumstances where the competition advocate has no legal connection with the legislative body. For example, the federal antitrust enforcement agencies have no jurisdictional connection with state legislators, yet correspondence, reports and testimony by the expert agencies can influence state policy.¹²

For the past two decades, FTC staff have extensively analyzed the impact of two types of state laws that have the potential to increase retail gasoline prices: laws regarding “divorcement” and “below-cost” retail gasoline sales. Divorcement laws limit the ability of refiners (and sometimes marketers) to own and operate their own gasoline stations, either statewide or within a certain distance of existing stations operated by franchised dealers. Laws banning below-cost sales prohibit the sale of gasoline below some statutorily-defined definition of cost B sometimes accompanied by a caveat that such sales are only illegal when they would harm competition.

FTC staff have opposed divorcement laws on the ground that they may increase prices and reduce customer convenience by forcing some refiners or marketers to adopt a particular retailing method, sale through franchised dealers, which economic research shows has led to higher costs in certain circumstances. Indeed, the most carefully-executed study of divorcement’s effects was authored by a senior FTC economist.¹³ FTC staff’s most recent advocacy letter on divorcement was addressed to Governor George Pataki of New York, who asked for the FTC’s views on a divorcement bill passed by the New York legislature in June 2002.¹⁴ He vetoed the bill in December 2002.

FTC staff have an equally lengthy record of opposing state legislation banning “below-cost” gasoline sales. Such laws at best duplicate laws against predatory pricing; at worst, they outlaw price-cutting that would not be considered “predatory” under antitrust standards. Governor Pataki sought the FTC’s views on this type of legislation in New York in 2002; he has not yet made a decision on the bill that the legislature passed. Earlier in 2002, however, a Virginia

¹²Besides the example below, the FTC has engaged in an extensive effort to inform states of competitive effects of various state legislative initiatives involving electric utility restructuring. See, e.g., Comment of the Staff of the Bureau of Economics of the Fed. Trade Comm’n, Restructuring in the Electric Utility Industry, No. 26427 (Ala. Pub. Serv. Comm’n filed Jan. 8, 1999).

¹³ See Michael G. Vita, *Regulatory Restrictions on Vertical Integration and Control: The Competitive Impact of Gasoline Divorcement Policies*, 18 J. REG. ECON. 217 (2000).

¹⁴ See Letter from Joseph J. Simons, Director, Bureau of Competition, et al., to Governor George E. Pataki (Aug. 8, 2002) <<http://www.ftc.gov/be/v020019.pdf>>. Footnotes in the letter contain an extensive list of past FTC advocacy on this issue.

House of Delegates committee voted to defeat a bill banning “below cost” gasoline sales after a committee member presented an analysis of the bill he requested from FTC staff.¹⁵

Antitrust Division usually works to affect competition policy through enforcement of federal antitrust laws or intervention in other regulatory processes, rather than by conducting studies. However, the Division sometimes undertakes studies and write reports concerning the state of competition and regulation in some industry sectors. These studies can form the basis for legislation. For example, in the early and middle 1980s the United States Congress became interested in reexamining the need to regulate oil pipelines and other oil facilities such as offshore lightering facilities.¹⁶ Despite their natural monopoly characteristics, U.S. oil pipelines face significant competition in many markets. New oil pipelines sometimes are constructed to compete with existing pipelines. Moreover, oil pipelines in some port areas face competition from river barges and ocean going tankers. In crude origin markets, pipelines may also compete with local refineries. In crude destination markets, crude oil pipelines may compete with local crude oil producers. Likewise, in product origin markets, product pipelines may compete with local marketers of product, while in product destination markets, product pipelines may compete with local refineries.

In 1986, the Division issued a report titled *Oil Pipeline Deregulation* advocating deregulation of some pipelines.¹⁷ The report explained the method of economic analysis used by the Division to formulate its position, listing criteria for assessing the costs and benefits of pipeline regulation. On the basis of its analysis, which included an examination of concentration ratios in major markets, the Division identified pipelines that should be deregulated, those that appeared to require some continued regulation, and those that were “too close to call.” The Division further called for deregulation for all new pipelines. In 1992, Congress passed legislation requiring the FERC to create a “simplified and generally applicable” method of rate making for oil pipelines to streamline proceedings and to deem all existing rates as just and reasonable (that is, allowed by law).

2. Commenting on Rulemakings: Minimizing Natural Gas Pipeline Regulation

Prior the the mid-1970's, the natural gas industry in the United States was vertically integrated between production and transmission via long term contracts between producers and interstate pipeline companies. In 1976, natural gas pricing was deregulated while natural gas transportation remained regulated by the FERC.¹⁸ The Antitrust Division became interested in the way that FERC was going to continue to regulate the natural gas pipeline companies which were now going to operate in both a competitive market (natural gas) and a regulated market (natural gas transmission). FERC issued a Notice of Proposed Rulemaking calling for comments

¹⁵ See Letter from Ted Cruz, Director of Policy Planning, *et al.*, to Hon. Robert F. McDonnell, House of Delegates (Feb. 15, 2002) <<http://www.ftc.gov/be/V020011.htm>>.

¹⁶ REPORT OF THE U.S. DEP'T OF JUSTICE, ANTITRUST ADVICE ON THE LICENSE APPLICATION OF THE TEXAS DEEPWATER PORT AUTHORITY (1979); REPORT OF THE U.S. DEP'T OF JUSTICE, OIL PIPELINE DEREGULATION (May 1986).

¹⁷ OIL PIPELINE DEREGULATION, *supra* note 16.

¹⁸ National Gas Policy Act, Pub. L. No. 95-621, 92 Stat. 3350 (1978).

on a proposal to significantly increase the separation of natural gas purchases and sales from transmission.¹⁹ Rather than comment on the specific regulations to implement the process of de-integration of gas sales from transmission, the Division set forth an economic framework in which the FERC could assess the comments it received and analyze the competitive impacts of its ultimate decision.

The Division noted that partial deregulation of a multi-product firm with monopoly power in one product may provide the opportunity and incentive for evasion of regulation through either self-dealing, cross-subsidization or discrimination.²⁰ The Division described several options for dealing with regulatory evasion via discrimination. One option is to continue to strictly regulate the price of the bundled services. This option can limit the efficiencies gained through allowing one or more of the services included in the regulated bundle to be provided in a competitive market. On the other hand, this approach preserves any operating efficiencies, due to economies of scope, achievable only by the vertically integrated monopolist. Under this option, the regulatory agency would have a primary role in maintaining “reasonable” prices for delivered electricity. A second option is divestiture of the more competitive service. The divestiture option encourages potential gains from competitive bulk power sales at minimal regulatory cost. It may, however, sacrifice economies of scale that the other options do not. Under this approach, rather than regulation, the antitrust laws would be expected to play a significant role in encouraging and maintaining a vigorous competitive bulk power market. A third option is to “unbundle,” that is, force the regulated firm to “purchase” regulated services from itself on terms and conditions comparable to those available to competitors. Unbundling could justify deregulation, or market-based regulations, of some bulk power sales that otherwise might require strict cost-based regulation to assure reasonableness. Ultimately, the FERC adopted the final approach for the natural gas industry.²¹ This third approach contemplates roles for both the FERC and the antitrust laws to maintain a competitive bulk power market. FERC would be responsible for enforcing its comparability and access rules, but the antitrust laws could also

¹⁹ Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation, 56 F.R. 38372 (proposed July 31, 1991).

²⁰ Self-dealing refers to paying one’s unregulated affiliate supracompetitive prices for inputs, which artificially increases the rate base or revenue requirement. Cross-subsidization entails shifting costs associated with unregulated activities or less strictly regulated activities, into the regulated rate base. Such strategies would allow a natural gas pipeline company with monopoly power in transmission to raise its transmission rates above the actual costs of transmission, thereby raising the costs to other generators competing with the utility to sell electricity to utilities or to large industrial retail customers; the transmitting utility, however, continues to incur only its actual costs. Discrimination occurs when a monopolist, in effect, conditions the purchase of its regulated service on the purchase of its unregulated service, creating a “bundle.” This may allow the firm to charge a supracompetitive price for the bundle including both the regulated service and the unregulated service. Supracompetitive prices will persist if competitors, who would offer natural gas at competitive prices, cannot gain access to the regulated monopolist’s transmission services on terms similar to those the monopolist enjoys. As a result, the regulated firm may earn supracompetitive profits on the sale of the bundle, and the benefits of increased competition in natural gas sales may be reduced or lost.

²¹ Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation and Regulation of Natural Gas Pipelines After Wellhead Decontrol, Order No. 636, 3 Fed. Energy. Reg. Comm’n Rep. (CCH) ¶ 30,939 (1992)).

apply if regulatory evasion conduct amounted to monopolization or attempted monopolization of a bulk power market.²²

Of course, not all examples of regulatory evasion conduct violate the antitrust laws, nor do vertical agreements or acquisitions violate antitrust laws merely because an opportunity for regulatory evasion is created. First, the harm to consumers, though a matter of concern, may be limited to rate base padding without a substantial lessening of competition in any antitrust market. Such evasion may be prevented by effective regulation. Once Antitrust Division suspects that regulatory evasion resulting in a consumer injury has occurred as the result of conduct by an integrated utility, the Division has a number of options. It can refer the matter to FERC or local regulatory bodies that can implement changes in the regulatory scheme to remedy the offending conduct or structural concerns.²³ As the Department's comments to the FERC in connection with its gas inquiry state, the decision among these three regulatory options should be made by weighing the costs and benefits of vertical integration in the markets under examination.²⁴

3. Specific Case Intervention: Regulation of Electricity Pricing

Under the Federal Power Act, the FERC has the authority to regulate price, terms, and conditions of wholesale power transactions.²⁵ Such transactions consist of sales between generators of electricity and utilities or other companies that resell power to consumers. The FERC historically regulated wholesale electricity prices based on a combination of historical accounting costs and the cost of capital for companies of comparable risk. By the late 1980s and early 1990s, wholesale power markets in the United States became increasingly competitive and competitive procurement, as opposed to building regulated monopoly generating capacity, became an important means of acquiring long-term bulk power supplies. In the early 1990s, the Division advocated consideration of market-based pricing in the wholesale electric market, urging the FERC to approve negotiated rates rather than impose rates for wholesale bulk power when purchasers had competitive alternatives to the sale being reviewed.

²² 1984 Non-Horizontal Merger Guidelines § 4.23.

²³ The Division could also challenge as a Sherman Act Section 2 violation in federal court certain regulatory evasion conduct where the effect is exclusionary.

²⁴ Comments of the U.S. Dep't Of Justice in Response to Notice of Proposed Rulemaking, In Re Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation, No. RM 91-11-000 (Fed. Energy Reg. Comm'n filed Oct. 15, 1991) at 5. Both the Division and the FTC have filed comments on FERC proposed rules regarding similar issues raised in restructuring the electric industry. See Comment of the Staff of the Bureau of Economics of the Fed. Trade Comm'n, In the Matter of Promoting Wholesale Competition Through Open-Access Non-discriminatory Transmission Services by Public Utilities, Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Nos. RM 95-9-000 and RM 94-7-001 (Fed. Energy Reg. Comm'n filed May 7, 1995); Comments of the U.S. Dep't Of Justice, In the Matter of Merger Policy Under the Federal Power Act, No. RM 96-6-000 (Fed. Energy Reg. Comm'n filed May 7, 1996); Comments of the U.S. Dep't of Justice, In the Matter of Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities, Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Nos. RM95-8-000 and RM 94-7-001 (Fed. Energy Reg. Comm'n filed Aug. 7, 1995).

²⁵ See 28 C.F.R. § 0.40(b) and (g) (1993).

The FERC adopted the policy of market-based rates for electric companies facing competition yet its implementation in specific cases was not always consistent with its stated policy goal. The Division highlighted this inconsistency by intervening in a quasi-judicial administrative case and requested that the FERC reconsider a decision it had reached disapproving a wholesale power contract between United Illuminating Co. (“UI”) and UNITIL Power Corp. (“UNITIL”).²⁶ As required under the Federal Power Act, UNITIL and UI sought FERC approval for a wholesale power contract. The price for power in the proposed contract had been determined by open market bidding, rather than calculated pursuant to principles of cost-based regulation.²⁷ UNITIL had received over 80 proposals from 54 companies totalling 2,697 MW from 74 generating units.²⁸ After evaluation of the bids and negotiations with the bidders, UNITIL selected six proposals from five companies totalling 84 MW, including 30 MW from UI.²⁹ Nevertheless, a FERC Order had disapproved the contract, on the ground that UI had not opened its transmission system to third parties.³⁰ Such intense bidding for the sale to UNITIL ordinarily would compel the conclusion that the price accepted was competitive, and therefore “just and reasonable,” as required under the Federal Power Act.

To satisfy itself that the market-based price was indeed competitive, the Division considered the same factors it would consider in an antitrust investigation. It defined a market for the product at issue, determined who could compete in the market, and assessed ease of entry into the market.³¹ The FERC Order had revealed no evidence that UI’s transmission practices had in any way limited competition for the UNITIL contract, such as by denying access through UI’s transmissions system to a would-be competitor for the UNITIL contract.³² To the contrary, the record showed that UI had not denied transmission to any competitor that sought it.³³

Even if UI had excluded some potential bidders from access to its own transmission, in the circumstances of this case, the remaining non-UI dependent competition was sufficiently intense to assure that the contract price was competitive. Under those circumstances, UI’s transmission

²⁶ Petition of the United States Department of Justice To Intervene for the Purpose of Requesting Rehearing, United Illuminating Company, No. ER92-397-000 (Fed. Energy Reg. Comm’n filed July 31, 1992).

²⁷ *Id.* at 61.

²⁸ United Illuminated Co., No. ER92-397-001, 1992 FERC LEXIS 2046 (Fed. Energy Reg. Comm’n filed Aug. 28, 1992).

²⁹ *Id.* at 27.

³⁰ At this time, the FERC had not yet ordered all utilities to open their lines to third parties.

³¹ The Department’s method of competitive analysis is set out in the 1992 Merger Guidelines. This method of defining and analyzing markets is employed generally and not only in cases of mergers.

³² United Illuminated, *supra* note 28, at 14.

³³ *Id.*

practices could not have prevented UNITIL from contracting for electricity at a competitive price.³⁴

This intervention was cost effective, in part, because the intervention took place late in the proceeding. The Division did not have to expend resources to participate in the trial portion of the proceeding or to write briefs on arguing about disputed facts. Instead the Division argued the point of policy based on a fully-developed record.

4. Networking: Informal Contacts As Advocacy

Both the FTC and the Antitrust Division use a number of less formal means of advocating competition. For example, agency officials and staff attend and make presentations at industry workshops, seminars, and public hearings dealing with restructuring issues in the industry. The audiences at such meetings often include a wide variety of industry participants. The concerns and questions expressed in these meetings may help the agency understand reactions to its comments and improve its understanding of technological and organizational developments in the industry. Participation in industry workshops and hearings provide additional opportunities to build relationships with regular participants in such events. Participation may also provide the benefit of “showing the flag” in the sense that industry participants perceive that the agency is monitoring developments in the industry from a law enforcement perspective as well as from an advocacy perspective.

The agencies also have routine contacts with other national-level agencies interested in regulatory reform, including the FERC and, to a lesser extent, the Department of Energy. Antitrust Division and FTC staff meet with staff from these agencies quarterly on an informal basis to discuss topics relevant to them all. The interagency staff meetings are regularly attended by the high-level FERC staff and by the FERC Chairman’s assistant. The purpose of these discussions is not to influence any pending case, but to allow these agencies to share perspectives and concerns regarding energy policy. The process is not only a source of new ideas, but a means of ensuring that staff are not unintentionally and unnecessarily inconsistent in their approaches to energy policy.

Finally, the agency may seek to formally affiliate itself with organizations of regulators. The FTC, for example, became a member of the National Association of Regulatory Utility Commissioners (“NARUC”). Membership in NARUC allows FTC staff to participate on staff committees of NARUC. Often the NARUC staff committee members are members of the senior staff at state utility commissions. Senior staff at the state commissions often organize and conduct evaluations of restructuring options in their respective states. Membership in NARUC also brings the agency into contact with the researchers at the National Regulatory Research Institute (“NRRI”), an organization supported by NARUC. NRRI researchers frequently consult with individual state PUCs. Such contacts can create a source of invitations to comment on regulatory reform proposals and can provide occasional invitations to testify before regulators or legislative committees.

E. Competition Advocacy in the United States: Assessment

³⁴ The FERC granted rehearing and approved the contract on different grounds. Two dissenting Commissioners would have granted rehearing for the reasons stated in the Division’s petition. *Id.*

Developing an effective competition advocacy program takes time and attention; it is difficult, however, to assess the effectiveness of such a program. In major ongoing policy debates like those regarding the electric power industry, it is difficult to assess agency advocacy efforts because long and short-term effects may differ; moreover, it is difficult to isolate the effect of agency advocacy efforts because decision makers usually are influenced by many factors, not just agency advocacy efforts. In our view, the most profound effects of the Antitrust Division and FTC staff competition advocacy efforts probably concern FERC's increasing interest in structural rather than behavioral remedies for market power and transmission discrimination. Starting with comments regarding the natural gas pipeline industry, through the most recent advocacy efforts regarding restructuring of the electric industry, both agencies have encouraged federal regulators to consider creating structures that give appropriate incentives to companies rather than relying on behavioral rules that require intrusive regulation. Moreover, independent of their direct effect on policy, these efforts have created an atmosphere that allowed FERC to focus on structural issues. At the state level, FTC staff have filed over two dozen comments with state regulators. At both the state and federal level, advocacy efforts by the Antitrust Division and the FTC have focused on the importance of market power issues in regulatory reforms.

Advocacy efforts generally are more successful in the short-run in areas where the agency has existing acknowledged expertise; presents new, pertinent information; and proposes approaches that are consistent with the proclivities of decision makers. In the long-run, competition agencies can also be effective by setting out an alternative approach or perspective that decision makers can adopt if their original approach falls short of expectations. Advocacy tends to be less effective, even though it may be economically sound, where it conflicts with the strongly expressed self-interest of industry participants (including the regulators themselves). The role of advocacy in such cases may still be valuable in the long term by educating decision makers about the costs and benefits of their decisions, even if the regulatory decisions are not altered in the short term.

5. COMPETITION ADVOCACY IN THE AIRLINE INDUSTRY

ICN	COMPETITION ADVOCACY IN THE AIRLINE INDUSTRY						2003
	<i>Sectoral regulator</i>	<i>Competition advocacy provisions</i>	<i>Main role of Department of Transports in competition advocacy</i>	<i>Airline mergers referred to the competition authority</i>	<i>Complaints (anticompetitive practices)</i>	<i>Consultation of other administrative bodies</i>	<i>Indirect impact of 11 September on competition advocacy</i>
France	DGAC	No Art.410 of the Commercial Code (no specificity as regards competition law)	No formal role in the promotion of competition, but closely associated in the European transports and competition policies	Boeing/Jappesen case 2001	Yes	Yes	Air France privatization has been delayed, substantial expansion in low cost airlines, fares reductions.....
Ireland	CAR	The Competition Authority advocates for	No formal role in the promotion of competition, but regulates airport	No (recent Law)	Yes	Yes	Substantial expansion in low cost airlines, reduction in fares....

		advocates for competition across the whole of the economy	regulates airport and aviation terminal services charges (recent consideration of a competing terminal at Dublin Airport)				
Mexico		Aviation Law Art. 25 an 43. Law on airports Arts.68 and 70		1995: creation of Cintra referred to FCC		Cintra operation (FCC heard opinion of aviation authorities, market competitors, pilot unions, ground workers, committees of the Congress related to the air transport industry).	Sale of Cintra postponed...
United States	DOT		No formal role in the promotion of competition, but DOT notably controls slots allocation at slot-constrained airports, takes action against unfair methods of competition ...	Before 1989, participation of DOJ in DOT proceedings, advocating that DOT apply antitrust principles to protect competition. Participation of DOJ in evidentiary proceedings in Northwest Airlines/ Republic Airlines and TWA/Ozark Airlines cases. Since 1989, mergers and acquisitions in the airline industry have been fully subject to the antitrust laws and DOJ has had responsibility for reviewing them .	Yes	Yes	Airline companies' bankruptcies, crisis in the sector due to a drop in air traffic....

5.1. GENERAL DIRECTORATE FOR COMPETITION, CONSUMERS AFFAIRS AND FRAUD CONTROL (DGCCRF)

AIR TRANSPORTATION COMPETITION ADVOCACY

Introduction

Competition advocacy refers to the activities conducted by competition authorities so as to promote a competitive environment by seeking to influence other governmental entities and increasing public awareness of the benefits of competition. In France, this role is carried out by both the Competition Council (“*Conseil de la concurrence*”) and the General Directorate for Competition, Consumers Affairs and Fraud Control (“*DGCCRF*”).

The DGCCRF pursues these aims by discovering and analysing illegal agreements and abuses of dominant positions. It also examines mergers before proposing a decision to the Minister of Economy. Finally, it supports the opening up of regulated sectors such as air transport, telecommunications, electricity and gas to competition.

The *Conseil de la concurrence* pursues these aims by enforcing competition rules relating to cartels and abuses of dominant positions. It also gives its opinion on mergers when requested to do so by the Minister of the Economy. The Council can also be referred to in order to provide its opinion on any question of competition by the Government, parliamentary committees, local authorities, professional organisations, trade-unions or consumers.

The French competition authorities have been particularly active in the sector of air transport. After having described the evolution of that sector into a fairly competitive market (1), this paper will explain how the French competition authorities have played their advocacy role by favouring deregulation (2) and by fostering the application of competition rules (3).

1. The evolution of the air transport sector in a competitive environment

In France, the traditional operator *Air France* is still majority state-owned. This national company is in the same situation as other operators regarding competition rules. *Air France* has in the past benefited important capital contributions under the supervision of the European Commission. The EC authorization¹ imposed a series of conditions in order to avoid competition distortion between *Air France* and other European companies, including:

- A strict restructuring plan was imposed on *Air France* in order to improve its profitability.
- A holding company aimed at preventing any transfer of the aid from *Air France* to *Air Inter* was created.

¹ Commission decision of 27 July 1994, OJ L 254/73 of 30/09/1994.

- State aid rules did not allow *Air France* to take shareholding in other companies.
- State contribution should not be used to buy new aircrafts or open new routes or lower fares.
- The Commission also reviewed separately each part of the State aid².
- These obligations were waived in the end of the restructuring plan in December 1996.

Appeals were brought before the European Court of First Instance against the Commission's authorisation decision following which *Air France* had been granted a State aid of 20 billion French Francs³. The Court annulled the Commission decision for lack of justification of the reasons⁴ but confirmed the substance of the case.

In France like in other OECD countries, **there was in recent years a noticeable growth in the number and size of low cost airlines**. Such companies maintain their low costs by a number of strategies, including lower labour costs, direct marketing, yield management and «no frills» service. Observers of the airline industry are familiar with the significant consumer benefits that can result when a low cost company enters a market: fares drop and capacity and frequencies increase, sometimes dramatically. It is not unusual for a deep fare cut to double the demand for airline service on a city pair in spite of drawbacks of distant airports.

In 1996, *Easyjet* was the first low cost company to enter the French market, followed by *Ryanair* in 1997, *Buzz* and *Basiq Air* in 2000, *Goodjet*, *My TravelLite* and *Air Lib* in 2002.

In the beginning of 2003, low cost companies operate numerous air links from French airports. To quote the main three:

Ryanair operates 14 international links:

- From Paris-Beauvais to Milano-Bergamo, Shannon, Dublin and Glasgow,
- To London, from Strasbourg, Nîmes, Biarritz, Dinard, Perpignan, Carcassonne and Saint-Etienne,
- To Frankfurt-Hahn, from Montpellier and Perpignan,
- To Brussels-Charleroi from Carcassonne.

Buzz operates 19 domestic and international links:

- To London from Bergerac, Grenoble, Brest, Caen, Chambéry, Dijon, La Rochelle, Limoges, Paris, Poitiers, Toulon, Toulouse and Tours,
- To Bornemouth, from Bergerac, Paris and La Rochelle,
- Brest-Marseille, Bordeaux-Grenoble.

² Commission decision of 21 June 1995, OJ C 295/02 of 10/11/1995; Commission decision of 24 July 1996, OJ C 374/09 of 11/12/1996; Commission decision of 16 April 1997, OJ C 374/06 of 10/12/1997. See also Orders of the CFI, Cases T-236/95 and T-49/97 of 27 January 2000, ECR II-51.

³ Immediately after the ruling, the Commission adopted the same decision with an extended motivation (Commission decision of 22 July 1998, OJ L 63/66 of 12/03/1999).

⁴ CFI, Cases T-371/94 and 394/94 of 25 June 1998, ECR II-2405.

EasyJet operates 11 domestic and international links

- From Nice to Amsterdam, Bristol, Geneva, Liverpool, London and Paris,
- From Paris to Liverpool, London, Newcastle and Geneva,
- From Lyon to London.

Whereas *Ryanair* and *Buzz* mainly operate from small airports, *EasyJet* has been unable to date to increase the number of its routes from Paris-Orly airport due to a lack of slots.

The decrease in fares has been dramatic, leading *SNCF* (the French national railways company) to propose, as of 2003, lower prices to face competition from low cost companies. Indeed, train is the first competitor to air transport in France on routes in which fast trains exist, and railway transport is more competitive on the market of routes of less than 3 hours, as the following table shows.

Travel time by train	1h 30	2h	2h30	3h	4h	5h
Train market share (%)	100	90	80	60	45	20

In 2001 TGV's market share reached 71% for the West of France and 66% for the South-East area.

The trend is going on.

The intense advertising campaign from *SNCF* concerning the TGV (Eurostar, Thalys, Paris-Marseille...) as well as from low-cost airlines has greatly contributed to enhancing competition advocacy and competition culture in the relevant sector.

To answer these new competitive threats, *Air France* has recently decided to adapt its fares on domestic routes. Moreover, if the State still holds a little more than 50% of *Air France*'s capital, it envisages privatising the company within the next few months, which should allow it to face these new challenges. Its management autonomy had already been strengthened by law in 2001. The company is now managed like a private enterprise and is able to compete on international markets and to take part in international alliances. On the domestic market, *Air France* has acquired small French companies to feed its Paris-Charles-de-Gaulle's hub. On domestic main routes (e.g Paris-Nice, Paris-Marseille, Paris-Toulouse) other companies directly compete with *Air France*.

Because of its beneficial effects on competition and consumer welfare, DGCCRF strongly assures that new entry is not thwarted by anticompetitive behaviour by incumbent airlines. The French competition authorities will take great care to ensure that these benefits endure

for the future, and try to apply to other less competitive sectors the same advocacy principles that have led to the successful opening of the air transport sector.

2 A (DE)REGULATED SECTOR...

The air transport sector in the European Union was liberalised in successive stages through the adoption of EC Regulations and Directives. Since January 1993, all international air routes in the European Union have been opened up to all companies that hold a Community licence without any restrictions. Since April 1997, unconditional access to all domestic markets has been granted to all airlines in the European Union (EEC Regulations No 2407/92 and No 2408/92). Moreover, [Regulation EEC No 2409/92](#) stipulates that airlines are no longer required to submit their fares to the national authorities for approval.

Closely associated in the EC competition policy, and in the European transports policy, the French competition authorities and the Ministry of Transport take part in the work on the adaptation of EC rules and the implementation of European procedures. This action is often described in the mass media. This obviously contributes to explaining the active role of competition authorities in this sector like in others. In addition, competition authorities have to advocate competition principles when transposing relevant European law.

- Regulation No 2408/92 of 23 July 1992 on access for Community air carriers to intra-Community air routes.

One challenging aspect lies in the conciliation of opening up markets with regional development concerns, each of them deserving advocacy.

According to Article 4 of the Council Regulation No 2408/92⁵ on access for Community air carriers to intra-Community air routes: *"1.(a) A Member State, following consultations with the other Member States concerned and after having informed the Commission and air carriers operating on the route, may impose a public service obligation in respect of scheduled air services to an airport serving a peripheral or development region in its territory, any such route being considered vital for the economic development of the region in which the airport is located, to the extent necessary to ensure on that route the adequate provision of scheduled air services satisfying fixed standards of continuity, regularity, capacity and pricing, which standards air carriers would not assume if they were solely considering their commercial interest. (...) (d) If no air carrier has commenced or is about to commence scheduled air services on a route in accordance with the public service obligation which has been imposed on that route, then the Member State may limit access to that route to only one air carrier for a period of up to three years, after which the situation shall be reviewed. The right to operate such services shall be offered by public tender either singly or for a group of such routes to any community air carrier entitled to operate such air services."*

An equalization fund has thus been set up by two laws (December 29th 1994 and February 4th 1995), in view of compensating for selected air carriers' deficits.

⁵ Council Regulation (EEC) No 2408/92 of 23 July 1992 on access for Community air carriers to intra-Community air routes (OJ L 240, 24/08/1992).

Therefore French air carriers are free to choose as regards the opening of new domestic routes, which are operated on a commercial basis, if necessary by public tender.

- Regulation No 95/93 of 18 January 1993 on common rules for the allocation of slots.

This European Council Regulation⁶ sets common rules for the very sensitive allocation of slots at Community airports. Thus, Paris-Charles de Gaulle, Paris-Orly and Lyon-Saint-Exupéry airports are "fully coordinated airports", which means that at these airports, in order to land or take off, during the periods for which it is fully coordinated, it is necessary for an air carrier to have a slot allocated by a coordinator. Nice-Côte-d'Azur airport is a "coordinated airport", that is to say an airport where a coordinator has been appointed to facilitate the operations of air carriers operating or intending to operate in that airport.

In essence, there is a barrier to entry on the market when a carrier cannot obtain slots to operate on a chosen route or when available slots do not correspond to its wishes. At the four pre-cited airports, it is frequent that carriers applying for slots cannot get them. It is then the coordinator's responsibility to grant slots, taking into account "grand father's rights" and competition principles.

Article 5 of the same Regulation sets up "coordination committees" in fully coordinated airports, to assist, in a consultative capacity, the coordinator. Participation in this Committee must be open to at least the air carriers using the airport(s) regularly, the airport authorities concerned and representatives of the air traffic control. Article 8§4 provides for conditions according to which slots may be exchanged between air carriers or transferred by an air carrier from one route, or type of service, to another, by mutual agreement or as a result of a total or partial takeover or unilaterally. In France, slot purchases, loans and renting are not authorized. As an example, at Paris-Charles-de-Gaulle airport, *Air France* has nearly 50% of the slots, *Lufthansa* 4,5%, *British Airways* 3,5%, *Alitalia* 3%, *Europe Airpost* 2%, etc. In case of an air company bankruptcy, slots are reallocated by the coordinator.

- Council Directive No 96/67 of 15 October 1996 on access to the groundhandling market

The transposition⁷ into the French Civil Aviation Code of the Council Directive 96/67 of 15 October 1996 on access to the groundhandling market at Community airports has enabled the French competition authorities to advocate benefits of competition and bring about these topics during discussions with airport and airline companies.

Indeed, the Ministry of the Economy requested the *Conseil de la concurrence* to advise the French government on the transposition of the Directive and to check the decree proposal with respect to competition law⁸. On two points, the *Conseil de la concurrence* disapproved the proposal and asked for amendments. First, the *Conseil de la concurrence* insisted that the possibility of restricting the number of operators on the groundhandling market be strictly limited. It considered that the criteria of "the proper functioning and efficient use of the airport installations" was too vague. Airport authorities would have had too much leeway, which could

⁶ Council Regulation (EEC) No 95/93 of 18 January 1993 on common rules for the allocation of slots at Community airports.

⁷ Decree n°98-7 of 5 January 1998 modifying the Code de l'Aviation civile, OJ 07/01/1998.

⁸ Opinion of the *Conseil de la concurrence* n°97-A-24 of 12 November 1997, BOCCRF No 6, 31 March 1999.

have made anticompetitive behaviour easier. The French competition authorities therefore recommended changes in order to foster competition. Moreover, the *Conseil de la concurrence* promoted an amendment of the decree so as to allow a limitation of the number of operators only in those parts of the airport where it is necessary to do so. The French public authorities agreed to follow the *Conseil de la concurrence*'s opinion and the decree incorporated these two changes.

In this case, advocacy by the French competition authorities played an important role and strongly influenced the legislation applicable to the groundhandling market. The implementation of these provisions has fostered competition, chiefly in airports where groundhandling was previously a monopoly.

As a result, managing bodies of airports have progressively transferred such activities to third companies. These companies are generally chosen according to public procurement contracts rules. This new situation has strengthened competition on this market and fare cuts have often been observed, thus promoting competition. More than 150 French or European groundhandling companies are now active on French airports. To the extent that there are several service providers on that market in a given airport, fares vary and transport companies may now choose their providers according to prices and service quality.

DGCCRF and the *Conseil de la Concurrence* check that airport managers have no discriminatory behaviour or that their decisions are consistent with European competition rules (See decision n° 98-D 34; 2 June 1998 on groundhandling market at Paris-Orly Airport).

To date, DGCCRF has received no complaint relating to discriminatory behaviours or price policies, which might impede entry on the groundhandling market.

3....to which competition law applies.

According to Article 410-1 of the French Commercial Code (Book IV: Freedom of prices and competition), "*The rules established in this book shall apply to all activities of production, distribution and services, including those carried out by public persons, particularly under public service concessions*".

The French competition bodies consider air transport is not specific as regards competition law. This sector offers many opportunities for the competition authorities (DGCCRF and the *Conseil de la concurrence*) to intervene, most often in conjunction with the specialized supervisory authorities (mainly the *Direction générale de l'Aviation civile*-DGAC), to regulate concerned markets and allow their normal operation.

Moreover, notwithstanding sectoral European Council Regulations, European Community competition law is fully applicable to air transport services⁹.

⁹ ECJ, 30 April 1986, Case 209/84, ECR 1986, 1425 "Asjes".

Articles 81 and 82 EC Treaty and Articles 53 and 54 EEA Agreement apply to air transport services within the EEA as well as to air transport services between States which are not both members of the EEA (nevertheless, following the "effects doctrine" restraints of competition committed by parties located outside the EEA can be prohibited when it is foreseeable that they have immediate and substantial effects in the EEA). By Council Regulation No 3976/87¹⁰ of 14 December 1987 the European Commission was given power to adopt block exemptions to certain categories of agreements, decisions and concerted practices listed in Article 2(2) of the Regulation. Initially, the European Commission granted several block exemptions. Two out of these are still in force today: the block exemption on slot allocation and the block exemption on passenger tariff consultations, both recently renewed until 2005. The French competition authorities as well as the French Tribunals are competent to enforcing these block exemptions.

Parallel to Articles 81 and 82 EC Treaty and to these Regulations, national competition law is applicable to air transport services¹¹. This enables French competition authorities to advocate both at the international and domestic levels.

a) International level

Air France's acquisitions affecting trade between Member States have been subject to a strict review by the European Commission. Even before the entry into force of EC Regulation No 4064/89 on the control of concentrations, the European Commission examined the operation *Air France/ Air Inter/ UTA* so as to limit the anticompetitive effects of the operation¹². The French government, advocated by the French competition authorities, negotiated with the Commission in order to find the best remedies (*Air France's* divestment of *TAT*; commitments of the French public authorities to allocate slots to foreign companies).

b) National level

Merger control in air transport sector

To date, DGCCRF (responsible for merger control in France) examined two mergers concerning French air carriers: the acquisition of *Regional Airlines* by *Air France*¹³, the latter having a hub in Clermont-Ferrand (Center France) and the buy out of *Air Liberté* by *AOM*.¹⁴ In neither case, the Minister required an opinion from the *Conseil de la concurrence*. DGCCRF competitive analysis is in keeping with community law, including the definition of the relevant markets: the routes (city pairs origin-destination), hubs and networks.

Indeed, the DGCCRF has followed the complex approach adopted by the Commission and applied the so-called "point of origin/point of destination" (O&D) pair approach¹⁵. It also

¹⁰ OJ 1987 L 374/9, amended by Council Regulation (EEC) No 2344/90 of 24 July 1990 (OJ 1990 L 217/15) and Council Regulation (EEC) No 2411/92 of 23 July 1992 (OJ 1992 L 240/19).

¹¹ In cases of conflict, however, European competition law takes precedence, see ECJ, 13 February 1969, Case 14/68, ECR 1969, 1 (14) "Walt Wilhelm".

¹² See Commission press release IP/90/870 of 30 October 1990.

¹³ Letter of the Ministry of the Economy, Finance and industry to *Air France*, 27 April 2000; BOCCRF No 8, 25 July 2000.

¹⁴ Letter of the Ministry of the Economy, Finance and Industry to *Taitbout Antilles BV et Participations*, 29 September 2000; BOCCRF No 14, 30 December 2000.

¹⁵ According to this approach, every O&D pair should be considered to be a separate market from the customer's viewpoint. To establish whether there is competition on an O&D market, the Commission looks at the different

followed the distinction made by the Commission between “time-sensitive” and “non-time-sensitive” customers¹⁶. For instance, the Minister considered that lines such as Paris-Nice, Paris-Perpignan and Paris-Toulon constituted relevant markets.

An important point in both these cases is that the Minister considered that the strong position of the parties would not lead to anticompetitive effects because of the existence of potential competition. Moreover, in the *Air Liberté/ AOM* case, the French authorities reviewed potential collective dominance issues. The Minister considered that there was no risk of a collective dominant position between the new entity and *Air France* for various reasons such as the absence of any structural link between the new entity and *Air France* and the difficulty of a coordination of the tariffs. The *AOM* case has been one of the first decision on this topic.

Publication of these decisions in the "Bulletin Officiel" -BOCCRF contributes to competition advocacy and transparency towards other institutions and the public at large.

In another merger case concerning foreign companies (*Boeing* and *Jeppesen*¹⁷) DGCCRF decided to refer to the *Conseil de la Concurrence*. The Council reasserted that competition rules make no distinction as to the nationality or location of enterprises, and apply if the operation is likely to have effects on the national territory. The parties were not active on the same market but the issue of vertical integration was at stake. However, the *Conseil de la concurrence* suggested that this problem could be resolved through specific confidentiality agreements and was in favour of the authorisation of the merger. The Minister eventually authorized the merger, however making this clearance subject to the accomplishment of commitments made by the parties.

?Administrative and legal decisions

Many decisions have been issued by the French competition authorities in the air transport sector and fines imposed on operators who had infringed competition rules.

The French competition authorities have promoted competition culture amongst economic operators, professional bodies and national judges, by giving their opinion on competition issues arising in the sector.

In 2001¹⁸, the *Conseil de la concurrence* gave an opinion to a professional body representing operators active in the air transport of goods with respect to a professional agreement fixing a uniform rate for security measures applicable to this activity. The *Conseil de la concurrence*

transport possibilities in that market, such as the direct flights between the two airports concerned (or between the airports whose respective catchment areas significantly overlap with the catchment areas of the airports concerned), the indirect flights between the airports concerned at each end or other means of transport like road, rail or sea. Whether one of those alternatives is substitutable to the direct route depends on factors such as travel time, frequency or the price of the different alternatives.

¹⁶ Depending on their different requirements, the Commission distinguishes in principle between “time-sensitive” and “non-time-sensitive” customers. For the first group, time is of the essence, either as regards the need to ensure a minimum travel time or the need to travel at a precise time of the day, or both. Also, certain time-sensitive passengers may need to book a flight at short notice or require flexibility (the possibility to miss one flight and book onto the next). Time-sensitive passengers are willing to pay a premium to have their requirements satisfied. On the contrary, for non time-sensitive passengers, savings on the price of the trip have priority over time constraints.

¹⁷ Decision of the Minister of Economy, Finance and Industry of 4 July 2001; BOCCRF No 15, 23 October 2001; Opinion n°2001-A-10 of the *Conseil de la concurrence* of 12 June 2001; BOCCRF No 15, 23 October 2001.

¹⁸ Opinion of the *Conseil de la concurrence* n°01-A-07 of 28 March 2001.

considered that, even if this agreement was favoured by the French public authorities in order to meet new legal obligations imposed on operators, it constituted a cartel and was not likely to be exempted under competition law since an uniform rate was not necessary to maintain the security of air transport merchandise. The French competition authorities clearly advocated in favour of competition rules as far as these rules are compatible with the security of air transport.

The Conseil d'Etat (the supreme administrative Court) plays a key role in competition advocacy, not only as a judge and through its decisions' diffusion, but also as a consultative body to which the government often refers to, and by the fact that some of its members are also active in regulation bodies.

The Conseil d'Etat has the power of repealing decrees, orders or decisions from which anticompetitive practices stem from. The Conseil d'Etat is not entitled, however, to impose fines as can the Conseil de la Concurrence.

Moreover, an appeal is possible before the Conseil d'Etat against the Ministry of the Economy's merger decisions. Recent Acts have given the Conseil d'Etat the power of reviewing fines imposed by the ART (the Telecommunications Regulation Authority)¹⁹ and the CRE (the Energy Regulation Commission)²⁰.

When acting as a judge, the Conseil d'Etat may refer cases to the Conseil de la concurrence.

In 1999²¹, the *Conseil d'Etat* suspended its judicial procedure in order to be advised by the *Conseil de la concurrence* on certain points specific to competition rules. The case concerned the refusal by ADP (Orly and Roissy airports) to authorise EDA to occupy part of the airport in order to be able to propose car rental services to the airport customers. The *Conseil de la concurrence* was asked to determine and explain whether Orly and Roissy constitute separate markets with respect to car rental services²².

In France, when operating an economic activity on a given market, public entities must comply, as well as private enterprises, with competition law.

Since 1999 (a decision issued by the "*tribunal des conflits*", a jurisdiction competent to settle conflicts between public and private law), anticompetitive practices carried out in an airport are a matter for the Conseil de la Concurrence only if the public body or its representative is not operating in the framework of a public interest activity needing public powers. In the latter situation only administrative jurisdictions are competent.

Therefore, the Conseil de la concurrence is competent for dealing with abuses of a dominant position of public entities on a series of markets. Two recent examples concern *Aéroports de Paris* (ADP). ADP is a public corporation governed by French law and enjoying financial independence which, pursuant to Article L.251-2 of the French Civil Aviation Code, is responsible for the planning, administration and development of all the civil air installations that are centred in the Paris region, including Orly and Charles-de-Gaulle airports. It is in this field

¹⁹ See forthcoming French submission on Telecoms competition advocacy

²⁰ See forthcoming French submission on Energy competition advocacy

²¹ Conseil d'Etat, Société EDA, 26 March 1999, Requête n°202260.

²² The plaintiff eventually decided to stop the proceedings.

essential to make such an important economic agent respective of competition and to strengthen its « competition culture and awareness ».

The first case is known as the *TAT* case²³. *ADP* obliged *TAT* company to resort exclusively to *ADP*'s teams to operate the passenger-bridge driving services further to *TAT*'s transfer to Orly-Sud airport, even though *TAT* had its own personnel and this obligation had not been imposed on *Air France* when this company was based in Orly-Sud. This discriminatory behaviour was considered as an abuse of a dominant position.

The second example is also an *ADP*'s abuse of a dominant position. The relevant market was airport and peripheral hotels area. The Paris Court of Appeal considered as discriminatory *ADP*'s decision to authorize airport hotels' advertising while impeding peripheral hotels from placing boards, even in return of a fee.

As for it, DGCCRF checks public procurement contracts and public service concessions in order to prevent, stop or punish anticompetitive practices. For example, advisory action has recently been taken vis-à-vis the draft regulation on public procurement of *Aéroports de Paris*, thus contributing to competition advocacy.

²³ Cour de Cassation, 12 March 2002

5.2. IRISH COMPETITION AUTHORITY COMMENTS: AVIATION

1. Introduction

The legal framework in Ireland operates within the parameters set by the EU both for the aviation and competition. However, some of the competition and regulation issues that arise in other Member States, such as slot allocation, are not present in Ireland.

2. Legal Framework of Airline Industry

2.1 *International Air Transport Agreements*¹

Ireland has over 30 bilateral agreements with non-EU/EEA states. The most important of these bilateral agreements is with the US and, to a lesser extent, Canada.² These agreements typically designate carriers that can operate between the two states and the destinations they can serve. Although there are no open skies bilateral agreements the Irish authorities look sympathetically at requests to be included as an additional designated carrier. The purpose of these agreements is to encourage air services between Ireland and other states.

A particularly restrictive arrangement is in place for transatlantic flights.³ At least 50% of non-stop scheduled flights by each airline to/from the US to/from Ireland, within the same twelve-month period, must operate non-stop to/from Shannon. Prior to 1993 all flights had to stop at Shannon. Airlines are forced to use Shannon to a much greater extent than they otherwise would, inconveniencing passengers, raising costs and quite possibly reducing competition/entry on the transatlantic route. The so-called Shannon Stopover is designed to encourage development in the west of Ireland.

2.2 *Competition Law*⁴

Ireland's competition law is contained in the Competition Act, 2002. The substantive provisions mirror EU competition law with respect to anti-competitive agreements and abuse of a dominant position.⁵ The Act also provides for the direct application of EU law in Ireland in these two instances. While the merger procedures are modelled on the EU, the test for mergers is substantially lessening of competition rather than creating or strengthening a dominant position.⁶ The Competition Act, 2002, is a law of general application and thus covers air transport services.

¹ Based on discussions with the Department of Transport. Their website – www.gov.ie/tec/aviation - has details of the states with which Ireland has bilateral agreements.

² The transatlantic market accounts for 8.7% of all passengers using Irish airports.

³ These restrictions apply to both freight and passenger traffic.

⁴ More details of the Competition Act, 2002, can be found on www.tca.ie.

⁵ This has been the case since the Competition Act, 1991. However, there was no public enforcement until the Competition Act, 1996. The Competition Act, 2002, introduced a number of changes to increase the penalties for 'hard core' cartel offences and a number of measures to assist in gathering evidence. These became effective on 1 July 2002.

⁶ Under the Competition Act, 2002, the Competition Authority has sole responsibility for mergers, except those involving the media where the Minister still retains a role. These provisions of the Competition Act, 2002, which came into effect on 1 January 2003.

3. Competitive Situation of the Airline Industry

3.1 Airports, Market Size, and Passenger Flows⁷

There are three major airports that account for virtually all air passengers in Ireland – Dublin, Shannon and Cork. Of these Dublin is by far the largest accounting in 2001 for 77% of all passengers through Irish airports, with Shannon and Cork accounting for 13% and 9.6%, respectively. Aer Rianta, a publicly owned undertaking, owns all these airports.

The geographical market distribution of the 18.5 million passengers that use Irish airports is as follows for 2001:

Market	%
<i>Transatlantic</i>	8.7
<i>UK</i>	49.3
<i>Europe (excluding UK)</i>	32.5
<i>Domestic</i>	6.1
<i>Transit</i>	3.4
Total	100

Not surprisingly domestic air travel is relatively unimportant in such a small country as Ireland where other forms of transport are likely to hold an advantage. Given the closeness, large size and historic links through, for example, emigration the importance of the UK is to be expected. Of UK passenger traffic London accounts for 52%, some of which will be for connecting flights.

3.2 The Major Carriers

Aer Lingus is the national flag carrier.⁸ It was established in 1936 and is publicly owned. Staff account for 4.8% of Aer Lingus shares with provision for this to rise to 14.9%. In 1999 the Government announced that a decision had been taken to arrange an Initial Public Offering, but no date has been set. During 2001 the fleet size of Aer Lingus peaked at 39 aircraft. In the recent past Aer Lingus has sold non-core activities (e.g., Futura, a Spanish based charter airline) to concentrate on its scheduled airline business.

Aer Lingus provides passenger and cargo services to the UK, mainland Europe, the US and within Ireland. On the transatlantic routes Aer Lingus claims to be the market leader accounting for 40% of revenue in 2001. In serving these destinations it appears to operate a hub-and-spoke system with Dublin as the major hub.

Turnover in 2001 was €1,347 million down from €1,372 million in 2000. Employment in 2001 was 6,833 persons. Following 11 September 2001 (and the foot and mouth outbreak that occurred earlier in the year) the airline announced its Survival Plan to reduce costs (e.g., staff by a third), reduce capacity and stimulate demand through fare reductions. The Plan was unable to

⁷ The data in this section is taken from Aer Rianta, *Annual Report 2001*, p. 16 & p.67.

⁸ This discussion is based primarily on Aer Lingus, *Annual Report 2000* and *Annual Report 2001* as well as information on the Aer Lingus website, www.aerlingus.com.

avail of state aid since Aer Lingus had previously received considerable state aid for the purposes of restructuring, the European Commission refused to sanction further aid.

Aer Lingus operates its own frequent flyer programme, TAB. To the extent that its major competitors are Ryanair and British Midland into the important UK market, it seems unlikely that these airlines would want to join either TAB or the **oneworld** alliance to which Aer Lingus belongs.⁹ In the case of Ryanair it has a different business model to Aer Lingus that relies on low cost/no frills and hence does not offer frequent flyer programmes, while British Midland belongs to the rival Star alliance.

Aer Lingus became a full member of the **oneworld** alliance on 1 June 2000. Aer Lingus has codesharing arrangements with a number of these **oneworld** airlines – American Airlines, British Airways, Finnair and Iberia – as well as with two non-**oneworld** carriers – Crossair and KLM. Aer Lingus signed important bilateral arrangements with American Airlines and British Airways in 2000. The decision to join the **oneworld** alliance was taken after a 1999 government-sponsored report¹⁰ that also recommended major operational strategic alliances with American Airlines and British Airways.

Ryanair is the major low cost carrier operating on the Irish market and the EU.¹¹ It has provided considerable competition for Aer Lingus as well as substantially expanding the market by offering low cost airfares.¹² It was established in 1985 with a daily flight between Waterford and London Gatwick. By 1995 Ryanair had become the largest passenger carrier on the Dublin-London route. This is the busiest city pair in the EEA with close to 2.5 million passengers in 2000. Ryanair flies to a number of destinations in the UK as well as Paris and Brussels from Dublin. Following full EU transport deregulation in the late 1990s Ryanair began to establish basis in other parts of the EU. In 2000 Ryanair was the 10th largest international scheduled airline in Europe in terms of passenger numbers, slightly ahead of Aer Lingus.

British Midland. There are of course other carriers but available evidence suggests that Aer Lingus and Ryanair are the two leading carriers in terms of passenger numbers through Irish airports. In the important UK market the third carrier is British Midland, a UK based carrier. The Dublin-UK market shares in terms of passenger numbers in 2000 were Aer Lingus, 40%, Ryanair, 39%, British Midland, 13% and others 8%.¹³

3.3 Market Expansion and New Entrants

The Irish demand for air travel has expanded rapidly with the annual average growth rate in passengers using Irish airports of 11.2% over the period 1996-2000.¹⁴ This growth reflects the high levels of economic growth experienced since the mid-1990s combined with the income

⁹ Membership of this alliance means that passengers enrolled in Aer Lingus's TAB programme can earn points/rewards when flying with other **oneworld** member airlines.

¹⁰ Salomon Smith Barney, 1999, *Advice and Assistance in Relation to a Strategic Alliance for Aer Lingus*. Report to the Minister for Public Enterprise and the Minister for Finance.

¹¹ This paragraph is based on Ryanair, *Annual Report and Financial Statements 2001*, and other material on their website, www.ryanair.com.

¹² This is discussed in Sean Barrett, 2000, 'Airport Competition in the Deregulated European Aviation Market', *Journal of Air Transport Management*, pp.13-27.

¹³ These data are in Aer Rianta, *Annual Report 2000*, p. 23.

¹⁴ For details see Aer Rianta, *Annual Report 2000*, p. 75.

elastic nature of air travel. Ireland's GDP per capita compared to the EU average ('100), for example, has gone from 79.9 in 1992 to 118.5 in 2000 and is projected to reach 127.5 in 2002.¹⁵

Existing airlines and new entrants have satisfied this additional demand. Indeed, those new entrants that charge low prices are frequently concentrating on a part of the demand curve that national flag carriers had to a large degree neglected. New entry into Irish airports is facilitated by incentive schemes offered by Aer Rianta to encourage passenger growth¹⁶ and the fact that Dublin, Shannon and Cork are not slot constrained.

The most recent entrant in terms of low cost carriers was Go, a UK carrier that was purchased in 2002 by EastJet. Go entered on the Dublin-Glasgow and Dublin-Edinburgh routes in 2000. However due in part to the competitive response of Ryanair in terms of low fares, Go withdrew from those routes in 2001.¹⁷ Other entrants have included Virgin on the Shannon- London Gatwick route.

It appears that information on passenger traffic, the number of carriers, their identity (e.g. national flag carrier or low cost carrier) and market shares on particular routes between Ireland and other Member States is not readily available.

ADVOCATING COMPETITION IN THE AIRLINE INDUSTRY

The Competition Authority

The Competition Authority has a function to advocate for competition across the whole of the economy. The Authority has the following general advocacy powers as set out in Section 30(1) of the Competition Act, 2002:

(a) to study and analyse any practice or method of competition affecting the supply and distribution of goods or the provision of services or any other matter relating to competition (which may consist of, or include, a study or analysis of any development outside the State);

(b) to carry out an investigation, either on its own initiative or in response to a complaint made to it by any person, into any breach of this Act that may be occurring or has occurred;

(c) to advise the Government, Ministers of the Government and

Ministers of State concerning the implications for competition in markets for goods and services of proposals for legislation (including any instruments to be made under any enactment);

¹⁵ See European Commission, 2001, 'Statistical Annex', *European Economy*, Number 72, Table 9, pp.130-31. The GDP comparisons are based on a purchasing power parity basis.

¹⁶ These can be found on Aer Rianta's website (www.aerrianta.ie) while they are also discussed in Sean Barrett, 2000, 'Airport Competition in the Deregulated European Aviation Market', *Journal of Air Transport Management*, pp.13-27.

¹⁷ Based on various newspaper reports. It should be noted that the Chief Executive of Ryanair claimed that Go withdrew because of the high cost of operating from Dublin.

- (d) to publish notices containing practical guidance as to how the provisions of this Act may be complied with;
- (e) to advise public authorities generally on issues concerning competition which may arise in the performance of their functions;
- (f) to identify and comment on constraints imposed by any enactment or administrative practice on the operation of competition in the economy;
- (g) to carry on such activities as it considers appropriate so as to inform the public about issues concerning competition.

In addition to this the Minister may request that the Authority carry out a study along the lines of Section 30(1)(a). Under the original 1991 Act, this was the sole advocacy power directly given to the Authority. This was expanded under the 1996 Act to enable the Authority to conduct an own initiative study.

The Commission for Aviation Regulation

The Commission for Aviation Regulation has the following principal functions as set out in Section 7 of the Aviation Regulation Act, 2001. The Commission for Aviation Regulation (CAR) is to regulate airport charges and aviation terminal services charges in respect of airports having an annual passenger throughput in excess of one million passengers. The CAR has no formal role in the promotion or the advocacy of competition.

The CAR may provide for a different maximum level of airport charges at different airports. In the case of an airport authority, which manages more than one airport, the CAR may make a determination in relation to any one of the airports with reference to the aggregate of amounts levied by way of airport charges at that airport and amounts levied at the other airports.

The CAR must make a determination in relation to airport charges within 6 months of being established. Such a determination may provide

- for an overall limit on the level of airport charges
- the limits to apply to particular categories of such charges, or
- for a combination of any such limits.

The CAR's determination may operate to restrict such charges, or require reductions in them, whether by reference to a formula or otherwise and may provide for different limits to apply in relation to different periods of time within the 5-year price control.

In making a determination the CAR is charged with the aim of facilitating the development and operation of cost-effective airports, which meet the requirements of users. In pursuing this aim the CAR shall have due regard to the following factors.

- (a) the level of investment in airport facilities at an airport to which the determination relates, in line with safety requirements and commercial operations in order to meet current and prospective needs of those on whom the airport charges may be levied,

- (b) a reasonable rate of return on capital employed in that investment, in the context of the sustainable and profitable operation of the airport,
- (c) the efficient and effective use of all resources by the airport authority,
- (d) the contributions of the airport to the region in which it is located,
- (e) the level of income of the airport authority from airport charges at the airport and other revenue earned by the authority,
- (f) operating and other costs incurred by the airport authority at the airport,
- (g) the level and quality of services offered at the airport by its airport authority and the reasonable interests of the users of these services,
- (h) the cost competitiveness and operational efficiency of airport services at the airport with respect to international practice,
- (i) imposing the minimum restrictions on the airport authority consistent with the functions of the Commission, and
- (j) such international obligations as are relevant to its functions.

The Competition Authority made a submission to the public consultation on the issue, which is available on the CAR's website (www.aviationreg.ie).

The CAR made its determination in August of 2001, where it decided that only 27% of Aer Rianta's proposed five-year €1.3bn investment programme was justifiable¹⁸. This determination is currently under appeal by Aer Rianta who claims that the Commissioner acted in excess of his powers.

Pursuant to Section 34 of the Competition Act, 2002, the Authority concluded *a co-operation agreement* with the CAR on the 19th December 2002. The purpose of this agreement is to facilitate co-operation, avoid duplication and ensure consistency between the actions of the Authority and the bodies concerned.

The Department of Transport

The Minister for Transport also has an important role in relation to promoting competition in the aviation sector. Recent initiatives include the serious consideration of a competing terminal at Dublin Airport (a report recommending that a competing terminal be built at Dublin was recently placed before the Government) and there has been some discussion of splitting up Aer Rianta (the State company that owns all 3 airports that are regulated by the CAR).

Interventions of the Competition Authority

Proceedings

The Competition Authority has taken no proceedings with respect to predatory pricing, excessive pricing, or frequent flyer programmes since it was given enforcement powers in 1996. No airlines mergers have been referred to the Authority by the relevant Minister for consideration.

¹⁸ The Determination is available at www.aviationreg.ie

Although between 1991 and 2002 undertakings could notify agreements to the Authority none were received during that period relating to the airline industry.¹⁹

Prior to the internet as an effective way for selling tickets, particularly for low cost airlines, travel agents were a very important outlet. Ryanair reduced the commission it paid travel agents. The agents, through the Irish Travel Agents Association, announced in April 1997 that they would not sell Ryanair tickets unless the company reversed its decision to reduce the commission. Searches of the premises of ITAA took place. The Authority instituted proceedings against the ITAA and a number of travel agents alleging that they were parties to an agreement/decision or concerted practice in breach of the Competition Act. In July 1998 the ITAA gave undertakings in the High Court that it would not continue to refuse to sell Ryanair tickets, as did the individual travel agents.

In 2002 a complaint was received that Aer Lingus (an allegedly dominant undertaking) had reduced the margin/commission payable to retailers. However, in this case, and in line with the approach outlined above, the Authority conclusion was that no abuse had taken place. In the Authority's Annual Report for 2002 the point was made that consumer welfare was either unchanged or improved. Furthermore, competition between different methods of distribution remained. Critically, while some undertakings may have been adversely affected by the alleged abuse, the purpose of the Competition Act is not to protect undertakings but to increase consumer welfare and promote competition.

These interventions to enable consumers to enjoy the benefits of reduced airfares represent one of the Authority's effective interventions into the airline market²⁰.

Complaints

There has been an instance of predatory pricing referred to the Authority.²¹ In 1999 Cityjet made a complaint to the Authority claiming it feared Aer Lingus might engage in behaviour which would constitute an abuse of a dominant position following the announcement by the latter that it proposed to commence flights between Dublin and London City Airport. A summons was issued to the Chief Executive of Aer Lingus requiring him to appear before the Authority and produce certain documents in January 2000. The Authority is in the process of finalising the file on this matter.

Slot Allocation

There are no capacity constraints at Dublin, Shannon or Cork so the issue of scarcity of landing slots and their allocation does not arise. However, the Commission for Aviation Regulation

¹⁹ This excludes one that related to a services agreement whereby an undertaking was granted the exclusive right to provide cargo handling, freight forwarding and freight management services, and related services at a small Irish airport – Knock International Airport. The agreement was approved by the Authority. Details of decision No 583, dated 29 February 2000, can be found on the Authority's website, www.tca.ie.

²⁰ The Authority intends to publish much more detail in relation to this investigation on its website in the coming weeks.

²¹ There were also allegations that the Ryanair in competing with Go had cut prices so low as to be involved in predatory pricing. See paragraph 3.12 above.

(CAR)²² considered whether Dublin airport should be ‘fully co-ordinated’ in a report dated 17 October 2001.²³ CAR decided that there were no serious capacity problems that could not be resolved in the short-term and thus there was no basis to designate Dublin airport as fully co-ordinated.

Priorities

The events of 11 September and the slowdown in the economic growth has led to severe cut backs in airline capacity, reduction in fares and poor financial results by the former national flag carriers such as Aer Lingus and substantial expansion in low cost airlines such as Ryanair combined with excellent financial results. The latter class of airlines seem to be able to expand despite slot constraints, concerns about predatory pricing and frequent flyer programmes. Are we therefore witnessing some sort of structural change in the airline industry that means the competition problems of the past need to be seen with a new perspective or are these traditional concerns mainly confined to the competition between the former national flag carriers?

In any event an important priority concerns the alliances and agreements among carriers such as the Star or **one** world alliances that may be used to create conditions that facilitate arrangements that can raise price and restrict entry. The benefits to consumers must be made clear and be quantified. It maybe that there are alternative less restrictive arrangements that deliver much the same level of benefits without raising the possibility of adverse consequences for competition.

²² The CAR is responsible for setting maximum airport charges, licensing Irish airlines subject to EU law, and deciding whether or not airports should be coordinated. The CAR was established as an independent regulatory agency in 2001.

²³ Commission for Aviation Regulation, 2001, *Decision on the Full Co-ordination of Dublin Airport*, Commission Paper 10/2001.

5.3. MEXICO: FEDERAL COMPETITION COMMISSION

ADVOCACY EFFORTS IN THE AIR TRANSPORTATION INDUSTRY

Background

At the beginning of the 80s as a result of financial problems¹, the stockholders of Mexicana sold 53% of their shares to the Mexican Government. The other national airline, Aeromexico (state-owned since 1959) also faced financial problems in this period, a cost reduction plan had palliative effects for half a decade.

The governmental control of the two main Mexican airlines lasted until the end of the decade of the 1980s. In 1988, a strike forced to Aeronaves de Mexico (Aeromexico) to file for bankruptcy. Government created a new company, Aerovias de Mexico, free of financial and labor liabilities. The airline was then sold to a group of domestic investors for US\$335 million. In the case of Mexicana, a new group of private investors capitalized the firm and acquired its control.

However the lack of experience of the new owners of both airlines led to bad management, for instance, planes were leased or acquired at unfavorable conditions² and the hiring of non-unionized personnel grew disproportionately. Mismanagement led both companies to enormous debts.

In 1991, the Mexican government process for granting concessions and permits to participate in the air transport industry became more flexible, which encouraged the entry of new airlines, like Taesa, that started operations using an aggressive commercial strategy. This firm and other competitors gained a modest market share in some routes.

Competition reduced fares and increased the number of passengers, but Aeromexico and Mexicana were not prepared to face this active competition which, added to the aforementioned financial troubles, caused an important crisis in both companies.

The Federal Law on Economic Competition (FLEC) was enacted on the 24th of December 1992 but came into force on the 22nd of June 1993. In February of 1993 Aeromexico requested authorization to the Mexican Government to invest in Mexicana, until then its main competitor.

The Ministry of Communications and Transports granted the authorization to Aeromexico for acquiring stock control over Mexicana but imposing several conditions on the transaction in order to preserve competition in the market.

Despite the acquisition of Mexicana by Aeromexico, their financial situation became worse and creditor banks took the control of both companies in September 1994. The ownership of the two major airlines by a single group of control placed at risk the the continuity of the service of air passenger transport.

¹ The growth of Mexicana was supported on short term debt in foreign currency, with the devaluation of Mexican peso in 1982, the financial situation of Mexicana turns critical.

² Mexicana signed a lease financing agreement with Airbus for the acquisition of 22 planes from September 1991 to May 1998 in addition to other leased equipment, calculating that the cost could be covered with a 40% occupation of each plane.

The crisis of the Mexican economy in 1995 caused a danger to the banking system; an important number of debtors became insolvent, the Mexican Government was forced to intervene in order to avoid the risk of bankruptcy in the bank system. The Mexican Government through the bank savings protection agency (current IPAB) assumed the bank liabilities generated for unpayable credits and took the control of several banks. The bank savings protection agency became then the holder of around of 65% of the stock of Aeromexico and Mexicana. Its stake comes from the capitalized debt of the airlines, held by troubled banks that were taken over by the government.

Cintra

In 1995, the banks that were managing Aeromexico and Mexicana notified the Federal Competition Commission (FCC) their intention to create Cintra, a holding for the shares of both companies. This “financial vehicle” would enable banks to capitalize liabilities of the airlines.

The banks claimed that their collateral could not be cashed due to different types of credit granted, and that capitalization of liabilities of airlines through a common shareholder was the only option for accomplishing the financial restructuring which, in turn, would enable them to recover their capital without affecting the industry.

Taking the above-described situation into consideration, the FCC allowed the temporary creation of Cintra, subject to the conditions of respecting a hold separate order and a set of other measures aimed at preventing abuses of market power.

The duration of Cintra was originally scheduled for a term of three years. Then the airlines would have to be put on sale separately. However Cintra filed an appeal before the FCC for a modification of the resolution, arguing that the three-year term established for the operation of the controlling company was insufficient to conduct an appropriate financial restructuring.

The FCC analyzed the reasoning of Cintra, heard the opinion of aviation authorities, market competitors of Cintra, pilot unions, flight attendants and ground workers. In addition, FCC consulted the committees of the Congress related to the air transport industry.

The FCC changed the term of three years of the former resolution to an indefinite term, but introducing several modifications to the original conditions and subjecting the companies to a close surveillance.

Once the financial restructuring was accomplished or in the event of failure to fulfill with the conditions imposed by FCC in the resolution, the companies were to be separated. Cintra consented to the term set by the FCC as well as to the procedure.

To ensure the fulfillment of the measures imposed by the FCC upon Cintra, a monitoring mechanism was designed. The FCC would periodically review the conditions of competition prevailing in the air transportation relevant market with the support of an independent consultant. As a consultant, Cintra chose one firm from a set of three options presented to it and approved by the FCC.

From the monitoring by the consultant, the FCC detected several domestic routes in which Aeromexico or Mexicana exercise market power (7 tourist routes and 19 business routes) and informed this situation to the transport regulator (Minister of Communications and Transport). In addition the FCC investigated the conduct of Cintra with respect to the fees charged to travel

agencies, granting cross guarantees and integration of the board of directors (the FCC ordered to Cintra that the boards of directors of Mexicana and Aeromexico must have different members). However, Cintra filed appeals and amparos³ for delay in the fulfillment of certain conditions.

Consultation

In 2000, the board of directors of Cintra, integrated by the bank savings agency (IPAB), several banks and the Ministry of Finance, filed a consultation before the FCC relative to their intention to sell Cintra.

The board of directors of Cintra considered that the sale of the company as a whole was the best option to maximize its value. In addition, the IPAB's mandate pursuant to Bank Savings Protection Law is to obtain the maximum income from the assets sale of the intervened banks.

The FCC answered the consultation according the next reasoning:

- The competition conditions in the market of air transportation have not changed since the resolution of the FCC about the financial restructuring process of Cintra. The subsidiaries of Cintra still have an important market share in the relevant market of the majority of domestic routes (In fact two competitors of the subsidiaries of Cintra, Saro and Taesa exited the market) and according the recent conduct of Aeromexico and Mexicana, these companies have market power.
- The normative barriers to entry, like the Foreign Investment Law and the Aviation Law impede foreign airlines to participate in the domestic air transportation market and foreign investment cannot exceed the 25% in the domestic airlines.
- The allocation of slots in major airports and other cost barriers impede the entry of new suppliers of the service.
- The efficiency gains from the integration of both airlines do not compensate the anticompetitive damage.
- The operation of two airlines in the domestic market of air transportation is financially and commercially feasible.
- The regulation and legal restrictions would reduce the value of Cintra in case of a joint sale of Aeromexico, Mexicana and its subsidiaries.
- The Ministry of Communications and Transport and the FCC would analyze a set of measures in order to avoid cutthroat competition.

In conclusion the best option is the separate sale of the assets of Cintra.

Addressing national interest and aiming to strengthen the competition, the FCC decided to make the following recommendations:

1. The joint sale of the companies, hence eliminating the effect of the conditions imposed on Cintra and its subsidiaries is contrary to the LFCE. To undertake such a joint sale

³ *Amparo* lawsuit is a legal action of last resort brought by an aggrieved party before a District Court or the Supreme Court of Mexico seeking reparation for, or the suspension or annulment of an act by a government authority that violates the complainant's constitutional rights.

would represent an operating merger of said companies that would create an agent with market power both in the majority of its routes and in the domestic market, protected from foreign competition and with limits to foreign investment. For these reasons the CFC will not authorize the joint and unconditioned sale of Aeroméxico and Mexicana, but will authorize their sale as independent competing companies. Selling the companies separately would eliminate the basis of the conditions imposed on Cintra in the August and November 1995 resolutions.

2. The information and facts examined infer that selling and operating *Aeroméxico* and *Mexicana* separately favor competition, are feasible and do not represent foreseeable dangers for development of the companies. Applicable legislation at any rate foresees mechanisms aimed at avoiding destructive conduct or practices in the domestic air transportation industry.

The recommendations of the FCC were accepted by the board of directors of Cintra and by the Congress Committees. However, due to the adverse development of the air transportation market caused by the events of the 11th of September, the sale of Cintra has been postponed.

5.4. UNITED STATES: DEPARTMENT OF JUSTICE

AIR TRANSPORTATION COMPETITION ADVOCACY

I. Airline Deregulation

Prior to passage of the Airline Deregulation Act of 1978, the U.S. airline industry was subject to pervasive regulation by the Civil Aeronautics Board. The CAB regulated fares, frequency of service, entry of new carriers, and expansion of existing carriers into new routes. As a result of this regulation, consumers had few choices for air transportation on most routes and fares tended to be high. The Antitrust Division of the Department of Justice was an early advocate of airline deregulation. The Division argued in speeches and testimony before Congress that relying on the competitive marketplace rather than government regulation would result in improved service and lower prices for consumers.

The Airline Deregulation Act of 1978 ended almost all the economic regulation of the domestic airline industry. Regulation of pricing and entry on domestic routes was eliminated and the process for certificating new entrant airlines was stream-lined. In addition, authority to grant antitrust immunity for agreements relating to domestic air travel was eliminated. The Act also provided that, after a phase-out period, airline mergers and acquisitions would be subject to the antitrust laws and under the jurisdiction of the Department of Justice.

The CAB functions that were not eliminated by the Airline Deregulation Act were transferred to the Department of Transportation. DOT retained authority to regulate airline safety, determine the financial fitness of carriers, issue operating certificates, and control the allocation of slots at slot-constrained airports. DOT also retained significant regulatory authority in the international aviation area, including allocation of restricted international route authority, approval of route authority transfers, and the authority to grant antitrust immunity for agreements relating to international operations. Finally, DOT retained authority to take action against unfair methods of competition in the airline industry, authority which it has used to regulate computer reservation systems and airline advertising practices. As discussed below, in those areas where DOT has retained jurisdiction, the Antitrust Division, acting under the general mandate of the antitrust laws, has taken an active role in advocating actions aimed at increasing competition in the airline industry.

II. Post-Deregulation Mergers and Acquisitions

From the enactment of the Deregulation Act until January 1, 1989, DOT retained jurisdiction over mergers and acquisitions in the airline industry. During this period there was significant consolidation in the industry, most of which did not raise significant competitive concerns. Where transactions did raise competitive issues, the Antitrust Division participated actively in the DOT proceedings, advocating that DOT apply antitrust principles to protect competition.

In 1985-86, DOJ participated in evidentiary proceedings held by DOT relating to two significant airline mergers -- Northwest Airlines/Republic Airlines and TWA/Ozark Airlines. DOJ participated in the proceedings as a party and submitted economic evidence. Both mergers involved significant overlaps at the airlines' hub airports. In the case of Northwest/Republic both carriers had hubs at Minneapolis, and in the case of TWA/Ozark both carriers had hubs at St. Louis. DOJ, analyzing the mergers using the Merger Guidelines approach, urged DOT to

disapprove both mergers. On many routes out of the common hubs, the merging airlines were the only or two of only three nonstop competitors, and, because no other airlines had significant presence at the hubs, there were no likely potential entrants. DOJ therefore concluded that the mergers would likely result in higher fares on many routes from St. Louis and Minneapolis. In both cases, DOT approved the mergers over DOJ's objections, basing its actions on a finding that connecting service and the threat of entry would constrain the merging carriers. Subsequent studies of the effects of these two mergers by DOJ economists and others concluded that the mergers had resulted in significant fare increases and reduced service in the city pairs where the mergers eliminated competition.¹

Since 1989, mergers and acquisitions in the airline industry have been fully subject to the antitrust laws, and DOJ has had responsibility for reviewing airline transactions under Section 7 of the Clayton Act and Section 1 of the Sherman Act.

III. International Immunity

A. International Alliances

In the early 1990s, the U.S. government began negotiating a series of bilateral "open skies" treaties with other countries. The open skies treaties removed restrictions on entry on routes between the U.S. and its treaty partners and reduced regulation of international fares. To encourage other countries to enter into open skies treaties, DOT adopted a policy of looking favorably on immunity applications for alliance agreements between U.S. carriers and carriers from open skies partners.

The central feature of alliance agreements is code-sharing between the partners on all or most of their systems. This allows the alliance partners to offer on-line service on many routes that neither would otherwise serve. For example, placing Lufthansa's code on United's Chicago-Portland flights and United's code on Lufthansa's Frankfurt-Berlin flights allows both carriers to sell on-line service between Portland and Berlin, which neither could offer independently. Alliance agreements also typically provide for various joint marketing activities (e.g., joint frequent flyer programs, joint bidding on corporate contracts) and efforts to reduce costs by consolidating some operations (e.g., sharing airport facilities).

DOT reviews applications for antitrust immunity under a public interest standard that requires consideration of the effects on competition and less anticompetitive alternatives to get any claimed benefits.² The statute also requires that DOT notify DOJ of the immunity application and give DOJ an opportunity to file comments.³ DOJ conducts its own independent investigations of these alliances, in some cases obtaining documents from the partner airlines. DOJ has actively participated in DOT's review of alliance immunity applications, most often

¹ Werden, Joskow & Johnson, "The Effects of Mergers on Price and Output: Two Case Studies from the Airline Industry," 12 *Managerial and Decision Economics* (1991); Borenstein, "Airline Mergers, Airport Dominance and Market Power," 80 *American Economic Review* 400 (1990).

² 49 U.S.C. § 41309.

³ 49 U.S.C. § 41309(c)(1).

through informal consultations with DOT staff, but in some cases by filing comments in DOT proceedings.

DOJ has not vigorously argued that antitrust immunity applications should be denied in their entirety, in light of DOT's considered judgement that immunity is a quid pro quo for open skies. In a 1998 proceeding involving immunity for an alliance between American Airlines and the Central American carrier TACA, DOJ filed comments arguing that the benefits from the alliance were fairly minimal because AA and TACA overlapped on a large number of US-Central America routes.⁴ While not arguing that DOT should disapprove the immunity application, DOJ urged DOT to carefully weigh the potential anticompetitive effects of the alliance against the very small benefits. DOT approved the immunity application.

DOJ has urged DOT to deny or limit immunity in specific markets where coordination between the partners is most likely to result in harm to consumers -- routes where the partners are the only or two of a small number of actual or potential competitors, typically routes that have hubs of the partners at both ends. In one of the early international alliance cases, United Air Lines and its Star Alliance partner Lufthansa sought immunity. DOJ conducted an investigation and concluded that immunity would likely harm consumers on two of the partners' hub-hub routes: Chicago-Frankfurt and Washington-Frankfurt. United and Lufthansa agreed with DOJ that they would not coordinate on fares for local passengers on those two routes. DOJ communicated this agreement informally to DOT, which included the "Carve-out" as a condition of the immunity grant.⁵

DOT has included similar carve-outs at DOJ's urging in a number of immunity orders, including American-Sabena (Chicago-Brussels), and Delta-Air France (Atlanta/Cincinnati-Paris). In a few cases, however, DOT has not limited immunity in overlap markets as advocated by DOJ. In 1995, Delta Airlines filed an application for immunity with three European partners (Swissair, Sabena and Austrian). DOJ determined that carve-outs from the immunity grant were warranted for six city pairs where Delta and its partners were nonstop competitors: Atlanta/Cincinnati-Zurich and New York-Brussels/Geneva/Vienna/Zurich. The airlines agreed to the Atlanta and Cincinnati carve-outs, but would not agree to carve out the New York markets. DOT issued an initial decision without the New York carve-outs and DOJ filed comments arguing that granting immunity to the only nonstop carriers in these markets would harm time sensitive passengers who did not view connecting service as a substitute.⁶ In its final order DOT rejected DOJ's position, finding that connecting service was in the market and that post-immunity entry was likely in the New York markets.⁷ DOT also placed great weight on statements by the airlines

⁴ Comments of the United States Department of Justice on the Order to Show Cause, Docket OST-96-1700 (Jan. 28, 1998). (<http://www.usdoj.gov/atr/public/comments/1779.htm>)

⁵ Order 96-5-27, Docket OST-96-1116 (May 21, 1996). (http://dmses.dot.gov/docimages/pdf8/9277_web.pdf)

⁶ Comments of the Department of Justice on Order to Show Cause, Docket OST-95-618 (May 28, 1996). (http://dmses.dot.gov/docimages/pdf8/9359_web.pdf)

⁷ Order 96-6-33, Docket OST-95-618 (June 17, 1996). (http://dmses.dot.gov/docimages/pdf8/9652_web.pdf)

that they would not implement their alliance if the New York markets were carved-out, jeopardizing the benefits of the alliance.

In one case, DOJ has advocated remedies to ameliorate competitive concerns arising from an alliance immunity application that extended beyond carve-outs. In 1997, American Airlines and British Airways, two of the largest carriers in the United States-UK market and two of the four carriers permitted to serve US-Heathrow routes filed an immunity application for their alliance. The US-UK market is the largest transatlantic aviation market and has historically been governed by one of the most restrictive bilaterals. An open skies agreement providing for open entry in US-UK markets therefore has the potential to create large consumer benefits.

DOJ conducted an intensive investigation of the proposed AA/BA alliance and concluded that without significant conditions immunity would result in serious competitive harm. The alliance partners were nonstop competitors on several important US-London routes and, due largely to the unavailability of slots to serve London airports, post-open skies entry would be unlikely to ameliorate these competitive harms. DOJ also concluded that there would be relatively few benefits from the alliance since both AA and BA already served a large number of US-UK routes. DOJ filed comments with DOT urging that, if immunity was to be granted, it be conditioned on divestiture of significant slots at London Heathrow to make new entry possible.⁸ DOJ also requested that routes where new entry was unlikely even with slots (routes between AA's Chicago and Dallas hubs and BA's London hub) be carved out from the immunity grant. Competition authorities in the EU and UK indicated agreement with the DOJ analysis that significant slot divestitures should be required. DOT did not issue a substantive decision in the proceeding, dismissing the immunity application because no progress was being made toward a US/UK open skies agreement.

In 2001 AA and BA again filed an immunity application, arguing that conditions had changed. DOJ again filed comments with DOT, arguing that significant slot divestiture was still required.⁹ DOT, in a tentative decision, largely accepted DOJ's position.¹⁰ AA and BA again withdrew their immunity application.

B. IATA

The International Air Transport Association (IATA) is a worldwide organization of about 280 member airlines (including the major U.S. airlines and all-cargo airlines such as FedEx and UPS). In 1985, the DOT granted approval antitrust immunity to IATA to meet and agree on passenger fares and cargo rates for international air transportation. The main justification for the grant of immunity was comity considerations.

⁸ Comments of the Department of Justice, Docket OST-97-2058 (May 21, 1998). (<http://www.usdoj.gov/atr/public/comments/1777.htm>)

⁹ Comments of the Department of Justice, Docket OST-2001-11029 (Dec. 17, 2001). (<http://www.usdoj.gov/atr/public/comments/9712.htm>)

¹⁰ Order 2002-1-12, Docket OST-2001-11029 (Jan. 25, 2002). (http://dmses.dot.gov/docimages/pdf75/151809_web.pdf)

A DOT proceeding to re-examine IATA's grant of immunity was opened in 1990. DOJ filed comments recommending that DOT withdraw immunity for IATA agreements on fares charged by U.S. airlines for tickets sold in the U.S. to consumers for travel to and from the US.¹¹ DOJ argued that the purpose and effect of the immunity is to raise prices to consumers, and that there are neither efficiency justifications nor public benefits from IATA's price-fixing. In addition, a blanket grant of immunity is overbroad and unnecessary, and the comity justifications lose force as more countries embrace deregulation and open skies. DOT has made no decision in the proceeding.

While IATA's grant of immunity has continued, DOT has acted to limit the immunity grant in some cases. In particular, in cases involving immunity applications for codeshare alliances, DOT has conditioned the immunity on withdrawal of the alliance carriers from IATA discussions relating to fares between the home countries of the alliance members and any other countries with immunized alliances.

IV. Rule-Making Proceedings

DOT has authority to issue regulations in a variety of areas affecting domestic airline operations. DOJ has actively participated in those rule-making proceedings that raise competitive issues, including regulations affecting computer reservation systems and the allocation of slots at certain airports.

In 1983-84 and again in 1990-92, the CAB and DOT conducted proceedings to consider comprehensive rules governing the operations of computer reservation systems (ACRSs"). These regulations raised serious competitive issues since the vast majority of airline tickets were sold through CRSs and the airlines that owned the CRSs had strong incentive to use them to limit competition. DOJ actively participated in these proceedings and advocated rules aimed at preventing airlines from using CRS ownership to exercise market power. The rules adopted by DOT included many of these provisions, including a bar on biasing displays to favor the flights of the owning carrier and a requirement that fees charged to airlines displaying fares in the CRSs be nondiscriminatory. More recently, DOJ supported a proposal by some smaller airlines to prohibit CRSs from enforcing parity provisions that forced airlines to participate in each CRS at the same level (i.e., to provide the same level of information and the same ticketing ability through each CRS).¹² DOJ argued that parity provisions eliminate competition between CRSs to provide enhanced services. DOT adopted a regulation prohibiting the enforcement of parity provisions.

DOT has authority to regulate the allocation of slots at the four slot constrained airports in the United States (O'Hare, Washington National, LaGuardia and JFK). DOJ has frequently consulted with DOT on ways to structure the slot rules in ways that encourage competition. In 2002, for example, DOT requested comments on various proposals to improve the allocation of slots at LaGuardia, including the imposition of fees for peak period flights, designation of slots

¹¹ Comments of the Department of Justice, Docket 46928 (Aug. 7, 1990); Reply Comments of the Department of Justice, Docket 46928 (May 14, 1992).

¹² Comments of the Department of Justice, Docket OST-1145 (Sept. 19, 1996). (http://www.usdoj.gov/atr/public/comments/crs_comm.htm)

for particular types of routes, and restricting slot usage to particular types of aircraft. DOJ filed comments arguing that the most efficient means of allocating scarce airport capacity through an auction system that would ensure that slots are put to their highest valued use.¹³ DOJ argued that peak pricing would be impossible to implement due to the absence of necessary information and that attempts by regulators to dedicate slots to particular markets or aircraft would result in inefficiencies. DOT has taken no action on the proposals, some of which would require legislation to implement.

¹³ Comments of the Department of Justice, Docket No. FAA-2001-9854 (June 20, 2002). (http://dmses.dot.gov/docimages/pdf82/177118_web.pdf)

6. OVERVIEW OF COMPETITION ADVOCACY IN THE LEGAL PROFESSIONS

A common feature in all of the countries reporting on advocacy with respect to the legal professions is the pervasiveness of government control of the sector. Consequently, most advocacy efforts were directed at laws and regulations, including amendments, at the draft stage, with the aim of trying to ensure the greatest role for competition.

In two jurisdictions there are a number of different disciplines that fall under the heading of legal professions: in France, huissiers de justice, notaires and greffiers des tribunaux de commerce as well as lawyers; in Switzerland, notaries and notaries public in addition to lawyers. The United States has only lawyers.

Both France and Switzerland have legislation at the national level that affects the legal professions and the competition agencies in both countries commented when there were major revisions to the laws in 1990 and 2000 respectively. In Switzerland there is comprehensive regulation at the cantonal level and the agency has been active when amendments to those laws have been proposed and has on occasion made suggestions when no changes were contemplated.

In the US, statutes and regulations that affect the practice of law exist at the state level and the US agencies have concentrated their advocacy on state and local bodies that were considering new rules that might have anticompetitive consequences.

The most frequently recurring topics of agency submissions have been fees, advertising and other rules of professional conduct, and issues concerning non-lawyers. In both France and Switzerland fees for certain of the legal professions are fixed by statute, a circumstance that the agencies have opposed. Cantonal legislation in Switzerland usually sets rigid fee scales for attorney services. Agencies in both countries have advocated for the loosening or elimination of these provisions and taken enforcement action when price-fixing strayed beyond the statutory system. Price-setting by lawyers is no longer acceptable in the US and any attempts would be subject to enforcement action rather than advocacy.

Various regulations in both Switzerland and the US have sought to limit advertising by lawyers and in both countries the agencies have argued that truthful non-deceptive advertising can contribute to competition without causing injury to consumers. Statutes that seek to regulate the “unauthorized practice of law” have frequently been proposed in the US and much of the agencies’ advocacy work in the legal professions has been focused on the effort to oppose any unnecessary restrictions. Examples of services that might not require the assistance of an attorney include real estate closings, tax advice, advice to tenants, estate planning and the provision of legal information but not advice. Similar issues have been faced as well in France and Switzerland where the agencies counseled against rules that would reduce competition among equally qualified providers.

On the question of the effectiveness of their advocacy efforts, it is probably fair to say that the agencies have reported that their efforts have been somewhat successful.

6.1. FRENCH MINISTRY OF FINANCE - DGCCRF

LEGAL PROFESSIONS AND COMPETITION ADVOCACY

Introduction

Competition advocacy refers to the activities conducted by competition authorities so as to promote a competitive environment by seeking to influence other governmental entities and increasing public awareness of the benefits of competition. In France, this role is carried out by both the Competition Council (Conseil de la concurrence) and the General Directorate for Competition, Consumers Affairs and Fraud Control ("DGCCRF").

The DGCCRF pursues these aims by discovering and analysing illegal agreements or cartels and abuses of dominant positions. It also examines mergers before proposing a decision to the Minister of Economy, Finance and Industry. Finally, it supports the opening up of regulated sectors such as air transport, telecommunications, energy and liberal professions to competition.

The *Conseil de la concurrence* pursues these aims by enforcing competition rules relating to cartels and abuses of dominant positions. It also gives its opinion on mergers when requested to do so by the Minister of Economy. The Council can also be referred to in order to provide its opinion on any question of competition by the Government, parliamentary committees, local authorities, professional organisations, trade-unions or consumers.

There is no official definition of professions in France, the only objective criteria being social (non salaried activities) and fiscal. Professions have common features (civil activity, high level of academic background and training, State laws and regulations specifying who may enter the profession, rules of ethic). Legal professions are no exceptions.

1-Advocacy and the regulatory framework

DGCCRF is a key stakeholder in the interministerial concertation which takes place prior to drafting laws or regulations aiming at ruling liberal professions.

In addition, the government must consult the Competition Council on any proposed regulation establishing a new regime the direct effect of which is to:

- 1) Place quantitative restrictions on the practice of a profession or access to a market;
- 2) Establish exclusive rights in certain zones;
- 3) Impose uniform practices with regard to pricing or with regard to selling conditions¹.

For instance, the Competition Council was consulted by the government in 1990 on the major reform reorganizing the legal profession². In particular, the Competition Council emphasised that, by prohibiting non-lawyers from providing certain legal services, certain provisions of the

¹ Article L462-2 of the Commercial Code

² Conseil de la Concurrence, avis n°90-A-01 relatif à l'avant-projet de loi portant réforme des professions judiciaires et juridiques, 4 January 1990, BOCCRF 22 February 1990, p. 82. See also the related opinion, Conseil de la Concurrence, avis n°97-A-12 relatif à une demande d'avis présentée par l'ordre des experts comptables, l'IFEC et autres portant sur la restriction d'exercice de leur activité professionnelle dans le domaine juridique, 17 June 1997, BOCCRF 18 November 1997, p.764

new law could prevent competition from these professionals despite their being as well qualified as lawyers.

A legislative or statutory framework may be an obstacle to competition authorities action against restrictions which arise directly from these rules. Indeed, practices which result from the application of a legislative or a statutory framework are not subject to competition rules³. It is notably the case for lawyer's advertising restrictions. On the other hand, competition authorities have a right to intervene where practices go beyond the legislative or statutory framework. The "Conseil d'Etat" (the supreme administrative Court) controls the lawfulness of this legal framework with regard to a set of rules that incorporates European competition law. In that manner, administrative courts also play an active role in competition advocacy.

Whereas fees of "officiers publics ou ministériels": "huissiers de justice" (Officers of the Courts⁴); "notaires" (notaries⁵), "greffiers des tribunaux de commerce"⁶ (trade tribunals' clerks, etc.) are fixed by decrees, professions are considered service providing activities and as such fall under the provisions of the Commercial code which "shall apply to all activities of production, distribution and services..."⁷

In this respect, French competition law does not differ from Community law, neither in its substance nor in its application. The fact that most liberal professions are organised as "ordres professionnels" (professional orders) is not an a priori obstacle to the application of competition rules against practices or decisions emanating from such orders. In that respect, the French competition authorities and the European Court of Justice have a similar approach.

Both judge that professional orders' decisions or practices can constitute concerted practices or agreements likely to be sanctioned for their anticompetitive object or effect, so long as they go beyond the framework of their general interest mission. This conclusion has been established in 2000 by the "Cour de Cassation" (the supreme judicial Court).

2- Advocacy and fees fixing

To date, competition rules have mainly been enforced in the field of fees.

Professional orders can commit anticompetitive practices, in particular when they seek to impose minimal prices. In 1979, the "Commission de la Concurrence" (Competition Council's forerunner) took action against recommendations issued by the Lawyers' order of Paris Bar concerning fees. These recommendations that took the form of hourly tariffs could be interpreted by certain lawyers and their clients as minima to be respected.⁸

³ Article L420-4 of the Commercial Code

⁴ Decree n° 67-18, 5 January 1967

⁵ Decree n° 78-262, 20 March 1978

⁶ Decree n° 80-307, 29 April 1980. Trade tribunals' clerks also have, however, non-fixed fees activities (e.g. *infogreffe services online*).

⁷ Article L410

⁸ Commission de la Concurrence, 19 November 1981, Ordre des avocats au barreau de Paris
Conseil de la Concurrence, decision n°96-D-78, 3 December 1996, Barreau de Tarascon-sur-Rhône
Conseil de la Concurrence decision n° 96-D-69, 12 November 1996, Barreau de Quimper

Cour d'Appel de Paris, 1ere ch., 9 December 1997, Bull. Joly Sociétés 1998, p. 378

Conseil de la Concurrence, Decision n° 96-D-79, 3 December 1996, Barreau de Rennes, Gaz. Pal. 14 et 15 mai 1997, p 15

On several occasions in recent years the Competition Council has sentenced lawyers orders' fees schedules on the ground that they distorted competition among the members of the profession by taking them off a fee calculation based on their costs and an individual strategy⁹. This jurisprudence has been plentifully confirmed by the Paris Court of Appeal.

It should be noted that, in most of these cases, the bar associations claimed that the fee recommendations were justified by consumers' interests. However, the French competition authorities considered that adequate information of the public could be achieved through the information provided by each lawyer to his client and should not lead to the adoption of a price list common to the whole bar¹⁰, which is anticompetitive and is, in fact, very detrimental to the consumer.

Furthermore, the Competition Council was consulted¹¹ by the government on the fixing of the fees of "huissiers de justice", whose functions are close to those of a bailiff. The Competition Council examined the fixing by the government of the fees in sectors where huissiers do not have a statutory monopoly and where some competitors operate. The fixing of the fees should be limited to those areas where huissiers are granted a statutory monopoly.¹²

3-Advocacy and compulsory insurance for the legal profession

The French Competition authorities' advocacy also concerns other aspects of the legal profession, such as the insurance obligation imposed on lawyers. For the purposes of protecting the consumer interests, the French law regulating the legal profession lays down an obligation for all lawyers to take out insurance covering their civil professional liability. As already

Conseil de la Concurrence, Dec n°s 98-D-01 et 98-D-02, 7 jan 1998 et déc n°s 98-D-05 à 98-D-07, 14 January 1998, Barreaux des Alpes-de-Haute-Provence, d'Aurillac, de Colmar, de Grenoble et de Marseille, BOCCRF 13 March, p.117s

⁹ Conseil de la Concurrence, dec. N° 2000-D-23, 31 May 2000, Barreau de Bonneville, BOCCRF 25 July 2000 p.416

¹⁰ See, for example, Conseil de la Concurrence, n°2000-D-52, 15 January 2001, Barreau de Nice, BOCCRF 23 February 2001, p.103

¹¹ See, for example, Conseil de la Concurrence, avis n°00-A-23 relatif à un projet de décret modifiant le décret n°96-1080 du 12 décembre 1996 portant fixation du tarif des huissiers de justice en matière civile et commerciale, 24 October 2000, BOCCRF 23 January 2001, p.5

¹² See Conseil de la Concurrence, avis n° 95-A-02 du 31 janvier 1995 relatif au projet de décret portant fixation du tarif des huissiers de justice en matière civile et commerciale.

mentioned, under article L420-4 of the Commercial Code, practices which result from the application of a legislative framework are not subject to competition rules. However, the Competition Council recently reaffirmed that competition rules apply to practices which restrict competition once they go beyond the relevant legislative framework¹³. Thus, bar associations are allowed to require the lawyers to take out collective insurance policy for their civil professional liability¹⁴ but any other insurance obligations, such as insurance covering damages due to natural disasters, fall under competition rules.

¹³ Conseil de la Concurrence, Décision n°03-D-03 relative à des pratiques mises en œuvre par le barreau des avocats de Marseille en matière d'assurances and Décision n°03-D-04 relative à des pratiques mises en œuvre par le barreau d'Albertville en matière d'assurances, 16 January 2003

¹⁴ Conseil de la concurrence, décision n° 03-D-03 op. cit, not yet published.

6.2. THE IRISH COMPETITION AUTHORITY

LEGAL PROFESSION: COMPETITION AND REGULATORY ISSUES

1. INTRODUCTION

This paper is in response to a request from the ICN's Case Studies subgroup no 3. It provides an outline of the legal profession in Ireland, including the regulatory framework governing this sector. It also outlines previous attempts at regulatory reform as well as discussing the current study being undertaken by the Competition Authority into several professions, including the legal professions.

2. INDUSTRY BACKGROUND¹

The legal profession in Ireland is divided into two distinct professional groups; solicitors and barristers.

2.1 SOLICITORS

The principal services provided by solicitors relate to advice and representation of clients in all aspects of the law. There is no area of the law in which solicitors cannot give advice, assistance or representation to their clients. Solicitors mostly do office work and represent their clients almost exclusively in the District Court, even though they have a right of audience in the Circuit Court, High Court and Supreme Court under the Courts Act, 1971.²

The most common areas of work carried out by solicitors include:

- conveyancing (the drawing up of legal documents for the purpose of transferring real property between buyers and sellers);
- trust and probate work (advising on and preparing wills, and administering estates and tax liabilities on death); and
- litigation (which includes arbitration and out-of-court settlements as well as court representation).

The provision of personal injury services covers both the office and court components of solicitors' work and anecdotal evidence suggests that personal injury work has grown rapidly in recent years. A range of other legal services and advice is also provided covering criminal and civil issues.

2.1.1 *Structure of the Solicitors' Profession*

Of the 2,035 solicitor firms in Ireland, 47% are single-solicitor businesses or sole proprietorships. The remaining 53% of solicitor firms are either principals (i.e. practices consisting of a principal solicitor employing one or more assistant/associate solicitors) or partnerships involving two or more solicitors. Very few firms employ more than 10 solicitors.

There are no restrictions on an Irish-qualified solicitor setting up a new practice as a sole trader in Ireland, although there are restrictions on normal competitive behaviour and on normal

¹ This section uses material published in "Indecon's Assessment of Restrictions in the Supply of Professional Services", prepared for the Competition Authority by Indecon International Economic Consultants-London Economics, March 2003. The Report is available from the Authority's Website at www.tca.ie.

² Solicitors often appear in the higher courts as assisting counsel.

commercial organisational form (there are also some restrictions on newly qualified solicitors from EU Member States establishing in Ireland). In Ireland, a newly qualified solicitor may establish a sole practice on the first day of qualification.

The law is uniform throughout Ireland as there are no federal or regional jurisdictions.

2.1.2 Requirements of a solicitor

Solicitors are free to provide advice and representation to their clients in all areas of the law and there is no limitation on the type of client who may retain a solicitor. As required by the self-regulatory body, the Law Society, solicitors need to be *independent*, *ethical* and *trained* in the substance and procedure of the law.

‘Independent’ means that the solicitor must be in a position to act for the client and the client only – the solicitor’s advice must be free of the interests of any third party. By ‘ethical’ is meant that the actions and advice of a solicitor must be the embodiment of integrity and above reproach at all times.

By meeting these fundamental requirements the solicitor has a duty not only to his or her client, but also an obligation to uphold the status of the profession more generally. In the process, it is argued, the solicitor contributes to the rule of law in society by acting as an intermediary between the State and the individual citizen.

2.1.3 Regulation of the Profession

Regulation of the solicitors’ profession is the responsibility of the Law Society of Ireland, the High Court (in particular, the President of the High Court), the Supreme Court (on appeal) and the Minister for Justice, Equality and Law Reform. The Law Society is the principal body responsible for the regulation of the profession on a day-to-day basis. Regulation is by way of statute and delegated legislation, principal among which are the Solicitors Acts, 1954 to 2002, and the Bye-Laws of the Law Society.

The governing body of the Law Society is the Council, which is provided for in the Charters of 1852 and 1888 and in section 3(1) of the Solicitors Act, 1954. Section 5 of the 1954 Act gives the Council the power to make regulations in relation to any matter referred to in the Solicitors Acts. Every regulation made under this provision must be laid before each of the Houses of the Irish Parliament. Thus, through the Council, the Law Society can initiate statutory change to the way in which the profession is regulated.

The Law Society traces its foundation to the granting of a Charter from Queen Victoria in 1852 (supplemented in 1888) and is concerned primarily with the education and training of solicitors and the continuing education of established solicitors. The Law Society is also responsible for the regulation of solicitors’ conduct, including solicitors’ accounts and clients’ monies, plus the Compensation Fund, which aims to ensure that a client who suffers loss as a consequence of the dishonesty or fraud of a solicitor (to whom the client has entrusted money) is compensated by the profession as a whole. The Fund complements solicitors’ professional indemnity insurance, which is a pre-requisite for practising as a solicitor in Ireland.

The Law Society is empowered to investigate complaints about solicitors and to monitor solicitors. Since the establishment in 1997 of the Office of Independent Adjudicator of the Law Society, a member of the public who is dissatisfied with the way in which his or her complaint has been dealt

with by the Law Society may apply to the Adjudicator for independent examination. The Independent Adjudicator may then direct the Law Society to re-examine the complaint or make an application to the Disciplinary Tribunal of the High Court, which may lead to the disciplining of a solicitor.

While there is no requirement for a solicitor to be a member of the Law Society in order to practise, the vast majority of practising solicitors are members. As of 31 December 2001, of the 6,030 practising solicitors in Ireland, 5,912 (98%) were members of the Law Society. As well as being part of a national network, the benefits of membership include various financial services schemes, pensions, venues for meetings, accommodation facilities and access to the Law Society's library.

The Law Society also provides technical information to its members, which, the Law Society submits, is ultimately to the benefits of clients of solicitors. The Law Society publishes a variety of booklets and pamphlets on particular legal topics.

From the beginning of July 2003, the Law Society will introduce a system of mandatory continuing professional development (CPD) under the Solicitors (Continuing Professional Development) Regulations, 2002. Solicitors will be required to undertake 20 hours CPD during a 'CPD cycle'. The first cycle will consist of 2 years and 6 months; cycles thereafter will consist of two-year periods. At least 15 hours are to be devoted to group study and up to five hours to private study. The system will be one of self-certification and will be a condition to renewing practising certificates of existing solicitors.

2.2 BARRISTERS

In the common law system,³ a barrister or barrister-at-law is traditionally defined as a lawyer qualified to plead in the higher courts. This is the norm in Ireland, where few solicitors take cases in the superior courts, namely the High Court and Supreme Court, even though they are entitled to do so in principle (under the Courts Act, 1971).

The distinction in the two branches of the legal profession is the result largely of tradition and has little or no statutory basis. The Bar Council is supportive of the distinction and points to its occurrence in many countries other than the common law group, where there are 'sitting-down' and 'standing-up' lawyers.

Cases are administered by solicitors, which includes the initial preparation of the paperwork (e.g. doctor's report, engineer's report), while barristers concentrate on pleading. Barristers are also responsible for the drafting of the legal documents for the case. With very limited exceptions, clients do not have direct access to barristers.

The key skill of barristers is advocacy. When pleading in any case, the advocate is bound by strict rules of conduct not to state his/her own view. Rather the function of the barrister is to present one side of the case with all the skills he/she possesses, so that the judge, or the judge and the jury, can compare his/her presentation with that of the counsel on the other side and then decide after full investigation where the truth lies.

The central place of practice of barristers in Ireland is the Law Library, which is housed at the Four Courts in Dublin. All practising barristers are required to be sole practitioners and accept

³ The common law countries are England and Wales, Ireland, the US (except Louisiana), Canada (except Quebec), India, parts of Africa, Australia and New Zealand.

work on the basis of the ‘taxi-rank rule’, which imposes an obligation on each barrister to act for a client where he or she is requested to do so. The rule often involves barristers acting in cases for unpopular clients or causes.

The profession also sometimes operates according to the ‘no foal no fee principle’, which, it is claimed by the Bar Council, provides all members of society with access to the superior courts.

2.2.1 Structure of the Barristers’ Profession

All practising barristers in Ireland are required to operate as sole practitioners so that the structure of the profession constitutes a fragmented sector comprising approximately 1,300 individual barristers. In practice, Junior Counsel work with Senior Counsel on particular cases but the non-concentrated nature of the profession is self-evident.

According to Bar Council figures, as of April 2002, there were 1,366 practising barristers in Ireland, of whom 83% were Junior Counsel (including ‘devils’ or ‘pupils’, i.e. members of the Bar under training), and the remaining 17% were Senior Counsel.

Members of both ranks of the profession can provide the same services. However, the Government-regulated Criminal Legal Aid scheme only applies to members of the Bar with more than six months practice, which is a requirement of the Code of Conduct of the Bar Council.

The Government is responsible for granting patents of precedence to barristers whereby they can then describe themselves as Senior Counsel (SC). It is a matter of choice for a barrister to decide to apply to the Government for a patent of precedence; such applications are typically made after ten or more years of practice as a barrister.

Apart from the distinction between Senior and Junior Counsel, there are no distinctions within the Bar, owing to the fact that each member is a self-employed sole practitioner. Each member is entitled to pursue his or her profession freely within any area of the law, throughout the country (and abroad, subject to local regulations).

While the country, by statute, is divided into circuits for the purpose of the administration of justice, there are no restrictions on barristers appearing in court or advising solicitors/clients in any of the circuits. Therefore, the market for barristers’ services is likely to be nationwide and barristers typically supply a range of legal services almost exclusively in the Circuit, High and Supreme Courts, although this is not to deny that some barristers specialise in certain areas (criminal law, taxation, commercial law, competition law) and base their practice areas in one circuit.⁴

2.2.2 Requirements of the Barrister

Barristers are also shaped by the same core values as apply to members of the solicitors’ profession, namely independence (a barrister’s advice to the client/solicitor must be free from the interests of any third parties so that there is no possibility of a conflict of interests), high ethical standards and client confidentiality (the common law principle of legal professional privilege applies to barristers as well as solicitors).

⁴ While the High Court sits in circuit as well as in Dublin, the Supreme Court sits only in Dublin.

2.2.3 Regulation of the Profession

Founded in 1541, the Honourable Society of King's Inns is the oldest institution of legal education in Ireland. Its principal activity is the education of new barristers, which is governed by the Education Rules of the Society. It is important to note that the Society is composed of members of the judiciary as well as members of the Bar. The governing body of the Society – the Council – has the power to change the rules governing the educational process and thus entry to the profession.

The Bar Council (founded in 1815) governs the training ('pupillage/devilling') requirements of the qualification process. It also governs membership of the Law Library, the central location of practice of barristers in Ireland. Through the Code of Conduct for the Bar of Ireland, the Bar Council has responsibility for regulating the conduct of practitioners and for regulating the organisational structure of practices. However, barristers employed outside the Law Library (by private companies or the State) are not members of the Law Library and therefore are not subject to its rules. Because they are not members of the Law Library, employed barristers (who are fully qualified) do not have the same rights of practice as practising barristers or members of the Law Library. Finally, the Bar Council is responsible for handling complaints about barristers by other barristers and others (e.g. solicitors) and has various disciplinary powers, although not the power to disbar, which rests with the Society.

In summary, the Bar Council is a self-governing regulatory body that is not governed by statute. It can, and does, modify the rules and codes under which the barristers' profession is regulated and governed.

3. REFORM ATTEMPTS AND LEGISLATIVE CHANGES

3.1 RESTRICTIVE PRACTICE COMMISSION AND FAIR TRADE COMMISSION REPORTS⁵

Prior to the enactment of the Competition Act, 1991, the Fair Trade Commission (previously the Restrictive Practices Commission) was responsible for advising the Minister for Industry and Commerce on competition matters in Ireland. Following Ministerial requests, the Commission undertook a number of studies into restrictive practices in various professions, including the legal profession⁶.

In these reports, the Commission set out its views on competition in the provision of professional services and made some specific recommendations in relation to restrictions in place within these professions. The approach of the Commission was to balance the need for Government to consider "circumstances where there may be a justification for the retention of certain professional restrictive practices" with the need for Government to "intervene in the public interest in order to seek the elimination of these restrictive practices".⁷

The Commission expressed the view that there were anti-competitive effects on the supply of professional services from the existence of fee schedules and advertising restrictions. In its 1982

⁵ This section uses material published in "Indecon's Assessment of Restrictions in the Supply of Professional Services", prepared for the Competition Authority by Indecon International Economic Consultants-London Economics, March 2003.

⁶ Restrictive Practices Commission (1982, 1985) and Fair Trade Commission (1990).

⁷ Restrictive Practices Commission (1987, p. 48).

report into the solicitors' monopoly on conveyancing in Ireland, the Commission also found that the monopoly constituted a restrictive practice and found no public interest reasons to justify this restrictive practice. The Commission also recommended that changes to the registration requirements at the Land Registry and to practices among lending institutions be made so as to give effect to its primary recommendation that sellers should have the right to employ non-solicitors to carry out their conveyancing work.

Finally, the Fair Trade Commission (1990) in its study of the legal profession noted that, in the context of restrictions to entry, the ability of the legal profession to exercise complete control over the numbers of persons admitted to the profession, and their qualifications, is quite likely to lead to a situation where the protection and promotion of the interests of those already within the profession become paramount. The Commission considered that any such self-protection would be likely to limit or restrict free and fair competition and would amount to an abuse of a dominant position which would be seriously disadvantageous to the common good, however much this might be claimed to be in the public interest.

3.2 LEGISLATIVE CHANGES⁸

The most relevant recent legislation has been the *Solicitors (Amendment) Act*, 1994, which, among other things, was (according to Shinnick, 2001) intended to break the solicitor's monopoly on conveyancing services. Other legislative proposals relating to the market for legal services were proposed in 1988, 1996 and 1998 and were in relation to advertising in the solicitors' profession.

One of the measures proposed to address the issues of standards and product liability in 1994 was the appointment of up to five lay members, nominated by the Minister, to the Disciplinary Committee of the High Court to represent the interests of the general public.

The measures that were proposed in the 1994 Bill that related to entry included:

- reducing the period of apprenticeship from a maximum of five years to a maximum of two years,
- reducing from seven to five years the minimum period of continuous practice required before a solicitor can take on an apprentice,
- permitting solicitors to have two apprentices instead of one and to have an apprentice for every two assistants, and
- permitting banks, insurance companies and other financial institutions to provide conveyancing and probate services.

These provisions were enacted with the notable exception of the provision that was intended to allow other organisations provide conveyancing and probate services.

Prior to the *Solicitors (Advertising) Regulations*, 1988, solicitors were forbidden to advertise their services or to undertake any activity that could be regarded as touting for business. This is because such activity was considered 'unprofessional' and would bring the profession into disrepute. Although the 1988 regulations did permit advertising of services, solicitors were still

⁸ This section draws on Shinnick, E. (2001) "Regulatory Reform in the Legal Profession: The Case of Ireland", presented at EUNIP conference at Austrian Institute of Economic Research, Vienna, Austria.

forbidden from specifying a fee or carrying out their practice in any way that may reasonably be regarded as touting or as attracting business unfairly. For instance, they could only claim superiority for the quality of their practice over those of other persons, if those other people were *not* solicitors.

The *Solicitors (Amendment) Act*, 1994 extended the 1988 regulations and permitted advertising of fees. This Act also stipulated that solicitors must provide clients with particulars in writing regarding actual charges or an estimate of charges at the outset.

The next two pieces of legislation, however, sought to place limitations on solicitor advertising. Shinnick (2001) states that the *Solicitor (Advertising) Regulations*, 1996 were intended to curtail misleading advertising. Such advertising focused on the claims of some solicitors that clients would only have to pay fees if they won civil actions for damages, generally advertised by making ‘no win no fee’ statements. The employers’ organisation, IBEC, and the insurance industry insisted that these claims contributed to a ‘compensation culture’. These regulations stipulate that solicitors must advise their clients that they could be liable for costs and expenses awarded against them by the courts if they lose.

The *Solicitors (Amendment) Act 2002* was introduced to prohibit advertising that referred to claims for damages for personal injury, either directly or indirectly. Shinnick contends that this Act was a response to concerns regarding claims made by army personnel for compensation for deafness arising from work activities. The belief was that this form of advertising, often referred to as ‘ambulance chasing’, had led to an increase in the volume of personal injury claims over the past 10 years and had brought the profession into disrepute.

3. RECENT DEVELOPMENTS⁹

In its recent review of regulatory reform in Ireland the OECD was critical of the regulations governing the legal profession, (OECD, 2001). Despite the recent reforms in the legal sector, there are, according to the OECD, unnecessary restrictions in the market for legal services in Ireland. The OECD is of the view that the relevant self-regulatory bodies, namely the Bar Council and the Law Society, should not retain control over entry to the profession and that restrictions placed on the form of ownership of legal firms should be liberalised.

Further reforms of the legal profession in Ireland suggested by the OECD were:

- Removing the restriction on non-lawyers providing conveyancing services;
- Making solicitors responsible for paying barristers and enabling clients to instruct barristers directly;
- Liberalising restrictions on business structures; and
- Suppressing publications, such as surveys of costs, which may be influencing fee levels.

⁹ This section uses material published in “Indecon’s Assessment of Restrictions in the Supply of Professional Services”, prepared for the Competition Authority by Indecon International Economic Consultants-London Economics, March 2003.

Along with its suggestion to remove control of entry to the solicitors' and barristers' professions by the Law Society and Bar Council respectively, the reforms would, in the opinion of the OECD, boost both efficiency and quality in the market for legal services in the State.

A report for the National Competitiveness Council and Forfás¹⁰ on the requirements for regulatory reform in the business services sector in Ireland also identified concerns in relation to the terms of entry to the legal professions, in particular the conditions affecting younger entrants. This report points to the rise in the educational and academic qualifications required to enter the legal profession over the past decade or two, which, in its opinion, has arisen as a consequence of the limited number of training places available at Blackhall Place (solicitors) and King's Inns (barristers). This in turn, according to the report, is because the self-regulating bodies are entirely responsible for the educational programmes and examination standards that determine entry to the profession. The report recommends that the Government should, in principle, move away from allowing self-regulatory bodies to control the educational programmes and examination standards governing entry to the professions.

In responding to the OECD report on Regulatory Reform in Ireland (2001), An Taoiseach (the Prime Minister) set out the Government's support for the regulatory reforms recommended by the OECD as a means to secure the progress Ireland has made over the past decade in economic and social development, in particular at a time when the economy is facing overall capacity constraints that could restrict future economic growth.¹¹ Irish Government policy is to support regulatory reform by eliminating unnecessary regulation, placing the emphasis on quality regulation and the application of competition policy to all relevant sectors as a tool of regulatory reform.

These factors have led to the commencement of a major Study by the Competition Authority into the need for regulatory reform in the professional services sector (see section 5.2).

4. COMPETITION AUTHORITY'S ADVOCACY EFFORTS

5.1 LEGISLATIVE AUTHORITY

The Authority has the following general advocacy powers as set out in Section 30 (1) of the Competition Act, 2002:

- to study and analyse any practice or method of competition affecting the supply and distribution of goods or the provision of services or any other matter relating to competition (which may consist of, or include, a study or analysis of any development outside the State);
- to advise the Government, Ministers of the Government and Ministers of State concerning the implications for competition in markets for goods and services of proposals for legislation (including any instruments to be made under any enactment);
- to publish notices containing practical guidance as to how the provisions of this Act may be complied with;

¹⁰ Forfás is Ireland's National Policy and Advisory Board for Enterprise, Trade, Science, Technology and Innovation.

¹¹ Department of An Taoiseach, Press Release: 'Taoiseach Responds to OECD Regulatory Report', April, 2001.

- to advise authorities generally on issues concerning competition which may arise in the performance of their functions;
- to identify and comment on constraints imposed by any enactment or administrative practice on the operation of competition in the economy;
- to carry on such activities as it considers appropriate so as to inform the public about issues concerning competition.

When determining whether to undertake a particular Advocacy Study, the Authority is mindful of the following factors:

- The economic importance of the sector or market;
- The intensity of competition;
- The existence of public or private barriers to entry;
- The degree of public interest; and
- The impact on Authority resources.

Under Section 30(2) of the Act, the Minister for Enterprise, Trade and Employment may request that the Authority undertake a study along the lines of Section 30(1)(a) within a given period of time. The Authority has complied with a number of such requests in recent years.

5.2 COMPETITION AUTHORITY'S PROFESSIONS STUDY

Following the release of the various reports that raised numerous regulatory and competition issues discussed above, the Authority decided that it would commence a study into several selected professions, including the legal professions.¹²

Following two rounds of public consultation, the Authority announced the Terms of Reference for its Study on 10 December 2001 and indicated that the study would cover competition in 8 professions in 3 sectors:

- Engineers and architects in the construction sector;
- Medical practitioners, veterinary surgeons, dentists and optometrists in the medical sector; and
- Solicitors and barristers in the legal sector.

The Terms of Reference for the study are:

- To study and analyse methods and practices affecting competition in the provision of certain professional services, with a view to identifying any potential or actual restrictions on competition, whether arising from legal provisions, professional rules or customs, or otherwise, that have an appreciable effect on competition.
- To identify and evaluate any consumer benefits claimed for any such restrictions and to consider whether the restrictions are proportionate to the achievement of any such benefits.

¹² No formal relationship exists between the Competition Authority and either the Law Society or the Bar Council.

5.3 PROGRESS TO DATE

In March 2002, Indecon International Economic Consultants were selected to conduct the main research phase of the study. Indecon's Report was published on 20 March 2003.

With respect to solicitors, the Consultants found that the key restrictions were:

- The Law Society's monopoly on the provision of professional education and training;
- Restrictions on the transfer of solicitors from other countries entering the Irish profession;
- Restrictions governing the transfer of Irish barristers to the solicitors' profession in Ireland;
- Selected restrictions on advertising;
- Restrictions on demarcation serving to give solicitors a monopoly in conveyancing and trust/probate services;
- Restrictions on lawyers based in other EU Member States competing with Irish solicitors in providing conveyancing, trust and probate services in Ireland;
- Restrictions on solicitors forming limited liability businesses; and
- Restrictions on solicitors forming multidisciplinary practices with other professionals.

With respect to barristers, it found that the key restrictions were:

- The King's Inns monopoly on the provision of the Diploma in Legal Studies course, which is a conversion course for non-law graduates and others (minimum age 25 years) wishing to be admitted to train as barristers;
- The King's Inns monopoly on the provision of the Barrister-at-Law (BL) degree course, which is the principal educational requirement to qualify as a barrister in Ireland;
- The pupillage requirements for new barristers, particularly the absence of remuneration for pupils;
- The prohibition on advertising by barristers;
- The prohibition on direct access to barristers by clients in contentious work;
- The solicitor-barrister distinction and solicitor-advocacy in the superior courts;
- The restrictions on barristers in employment from practising;
- The requirement that barristers operate only as sole practitioners;
- The prohibition on barristers forming multidisciplinary practices with other professionals.

5.4 THE REMAINDER OF THE STUDY

Following the Indecon Report, the Competition Authority will produce reports on individual professions in the following order: engineers, architects, dentists, optometrists, veterinary surgeons, medical practitioners, solicitors and barristers. This will involve:

- The publication by the Authority of Consultation Papers for each profession. These will include an analysis of the issues identified by Indecon and the Authority's draft recommendations.
- Responses will be invited, covering corrections of facts, correction of arguments presented for specific regulations, new arguments, or proposals for change.
- Oral hearings with interested parties may be held if the Authority deems it useful.
- The publication of a final report with specific recommendations.

It is envisaged that reports on the two legal professions will be finalised in 2004. On conclusion of the overall Study, the Authority may:

- seek changes to existing practices, present recommendations and where appropriate issue best practice guidelines to Government Ministers, relevant regulators, professional bodies and others with a view to the removal of unnecessary impediments to competition,
- publish information about markets or practices that improves knowledge and understanding of, or stimulates and improves competition generally in some or all of these sectors,
- offer a clean bill of health, or
- make recommendations for regulatory reform.

5. ASSESSMENT OF ADVOCACY EFFORTS

As outlined above, there have been several attempts at regulatory reform of the legal profession in Ireland, specifically the Restrictive Practices Commission reports over a decade ago and the various legislative changes introduced since 1988. As evidenced by the number of competition issues identified in the Indecon Report to consider the legal profession, these attempts have ultimately fallen short of ensuring adequate reform of the legal profession.

Despite the absence of satisfactory reform to date, the Restrictive Practices Commission report and the various legislative amendments, along with the OECD report on regulatory reform in Ireland, have all contributed to the debate surrounding the regulation of the legal profession. Furthermore, the introduction of the Competition Act 2002 has provided the Authority with a clear mandate in relation to advocacy. This provides some cause for optimism that reform in this sector may be possible by way of stimulating informed public debate and helping create a political will to undertake regulatory reform that would be beneficial for consumers.

However, this study is still progressing and the Authority has not arrived at definitive positions on the issues raised by the Indecon Report. Therefore, it is not yet possible to evaluate the Study's likely effectiveness.

6.3. SWITZERLAND COMPETITION COMMISSION

A. Legal professions. Background and structure

Notaries

1. In Switzerland, notaries are regulated at the cantonal level and exhibit large cantonal particularities. There are two types of notarial practices in Switzerland. In French-speaking cantons, a notary is classified as a liberal profession. In contrast, in most of the German-speaking cantons, notaries are, in keeping with the German tradition, notaries public i.e. civil servants of cantons or municipalities (Amtsnotar, Gemeindeschreibernotar). However, some German-speaking cantons increasingly admit the coexistence of the notary public and the liberal profession notary. In this situation, the two different types of notaries can have reserved fields of competency and competing fields that are determined by the cantons. In other cantons, there is no difference in terms of competency.

2. A law degree and a specific training period are prerequisites to becoming a liberal profession notary. This is not usually the case for the notary public. The Swiss citizenship is required in almost every canton for both types of notaries. Pursuant to the principle of territoriality, a notary can only exercise in the canton where he had obtained his license (with derogating inter-cantonal agreements).

ATTORNEYS

As well as the notaries, the attorneys are regulated at the cantonal level. There is though a federal law on the attorneys' freedom of movement which entered into force in June 2002. According to this law, attorneys don't need specific authorizations to represent in front of any court within Switzerland. The admissibility of foreign attorneys (EU/EFTA) is also part of this federal law. They have just to be registered in one of the 26 cantons.

B. Competitive objectives and regulatory changes to further these objectives

NOTARIES

3. The Federal Act on Cartels and Other Restrictions on Competition as of October 6th 1995 (hereinafter: Acart) does not apply to notaries for any "public activity", that is, for the activity of notarizing itself. In contrast, their "private activity" (for instance legal advice) is not exempted from the Act on cartels. In practice, however, it is very difficult to distinguish between the two activities since "private activity" is generally the correlate to "public activity" and takes place before it. A preliminary investigation carried out in 1997 by the Federal Competition Commission (hereinafter: Comco) concluded that notaries public are exempt from the Act on cartels pursuant to art. 3 of this law which excludes from the scope of applicability the publicly regulated markets.

4. The notaries are also not subject to the Federal Act on the Internal Market Law (IML) as of October 6th 1995 since they do not exercise a lucrative activity in the meaning of art. 1 §3 IML. This position has been confirmed by the Federal Supreme Court in a ruling of 30 June 1998.

5. The competitive objectives in this area are very limited since the Comco can only enforce (and with much difficulty) the Acart with respect to private activity (which represents only a

minor part of the earnings of notaries). The Comco has set a competitive objective to observe this protected market and to intervene through advocacy in the consulting procedure in case of the adoption of new cantonal legislation. Only very little regulatory changes have taken place in the notaries area. Nevertheless, the Comco advocated in the consultation phase of the revision of a cantonal law on notaries of Bern regarding the question of market sharing geographically with respect to the certification of property law acts. The Comco's opinion was followed.

ATTORNEYS

6. The major regulatory change to further the competitive objective in the area of legal professions is the Free Movement of Attorneys Act (FMAA) of 23 June 2000 that entered in force on the 1st of June 2002.

7. This new legislation introduces three main issues:

a) It provides for the free movement of attorneys within the Swiss territory. This new Federal legislation abolishes the necessity to obtain an authorization to represent a client for each legal proceeding in another canton. According to this new law, an attorney who wishes to represent clients in legal proceedings should be recorded in the attorneys' register of the canton where he has the seat of his practice. This registration in one cantonal register allows him to represent clients in legal proceedings in all Swiss cantons without the need for further authorization.

b) This law provides the main principles on which the rules of professional conduct applicable to attorneys are based. Of interest for competition in the legal profession is Art. 12 d. which provides that an attorney may advertise so far as this advertising is limited to objective facts and satisfies the public interest. These very broad principles will be rendered more specific by cantonal regulations. This reveals for instance that the freedom to advertise could vary a lot between the different cantons. Some cantons are more liberal than others.

Unfortunately Arts 8 d and 8 § 2 FMAA are very restrictive with respect to the notion of independence requested for the registration in the cantonal attorneys register. Attorneys in a salaried capacity are only allowed to be registered if they are the employee of another attorney who is himself registered or if they are employed by a "organization of public interest". In the latter case, attorneys can only represent clients in relation to the goal of the organization of public interest.

This restrictive provision to the entry in the register excludes from the rights of audience's monopole all the attorneys who are in a salaried capacity in public or private companies. This provision seems to restrict disproportionately the conditions of entry in the profession and distorts competition in favor of attorneys who exercise in a liberal form. The legitimate condition of independence refers more to the idea that the attorney must act independently in the interest of his clients without pressure from third parties. Independence must be interpreted in this sense to avoid conflicts of interest. A salaried capacity is usually not an obstacle to independence when the interests of the employer are not in conflict with the interests of the client. According to the case law of the Swiss Federal Supreme Court, there is a danger of conflicts of interests only when attorneys are employed in legal protection insurance (FSC 123 I 193). The Comco advocated in its opinion given in the consultation phase of the FMAA to adopt the interpretation of the Federal Supreme Court. The Comco's opinion was not followed by the Swiss Parliament. It is paradoxical that a law that is supposed to liberalize the legal profession is effectively more

restrictive than the jurisprudence of the Federal Supreme Court. It could be explained by the fact that among the MPs who voted for the law, a large percentage of them are themselves attorneys.

c) Lastly this new law facilitates practice of the profession of lawyers who obtained their license in a EU or EFTA States in Switzerland.

C. Source of authority to engage in advocacy

8. The Swiss Federal Act on Cartels and Other Restraints of Competition (Act on Cartels; Acart) of 6 October 1995 provides two advocacy provisions:

Art. 45 §2 Acart:

“The Commission may address recommendations to the authorities, the purpose of such recommendation being to promote effective competition, especially with regard to the drafting and enforcement of laws relating to economic affairs”.

Art. 46 Acart:

1. The secretariat shall review draft confederation legislation, especially in economic matters, that is likely to influence competition. It shall determine whether the effect of such legislation is not to introduce distortions or excessive restraints on competition.

2. In the consultation procedure, the Commission shall adopt a position with regard to the draft confederation legislation that limits or influences competitions in anyway whatsoever. It may issue opinions on draft cantonal legislation.”

D. Agency’s efforts over time

Advocacies in the attorney area

9. As a consequence of the FMAA, many cantons have begun to amend their regulations relating to attorneys. The Comco took this opportunity to review from a competition point of view the regulations relating to attorneys of all cantons. Through advocacy, the Comco seeks to bring more competitive aspects into these types of regulations at the drafting stage. The Comco can issue its own opinion in the consulting procedure of cantonal draft legislation but these opinions are not binding for the cantons. From 1999 to 2002, many opinions, pursuant to Art. 46 §2 Acart, were issued on proposed cantonal legislation for attorneys (for example cantons of Zürich, Schaffhausen, Tessin). When no amendment of the attorney legislation was contemplated, the Commission issued recommendations in accordance with Art. 45 §2 Acart (canton of Lucerne for instance). Three types of restraints on competition were singled out in the various opinions and recommendations of the Comco:

Scale of fees

10. First, numerous cantonal legislations in Switzerland provide rigid fee scales for attorney services. The Comco considers generally that rigid fee scales constitute a restraint on price competition. In the consultation phase of the FMAA, the Comco advocated without success to abolish fees scales in cantonal legislations. The fee scale provisions that were submitted to the Comco took the form of minimum and maximum hourly rates or a rate based on the value of a dispute (rate which varies with the economic importance of the transaction). Fees can only vary within this rigid framework depending on various criteria such as the complexity of the dispute, the responsibility of the attorney, the neediness of the client etc. These correctives were not

considered by the Comco as sufficient to ensure effective price competition between attorneys. The Comco advocates to cantons to adopt more liberal provisions on fees using the example of the provisions in the Geneva Canton which provides that "the fees, subject to the decisions of the commission of taxation, are fixed by the attorney himself taking into account work he has carried out, of the complexity and of the importance of the affair, of the responsibility he has assumed, the result obtained and the situation of his client". Attorney services provided in the frame of the legal aid are not concerned by this opinion/recommendation. Lastly, the Comco did not advocate to issue guidelines on fees since it has usually the effect that these guidelines are in practice followed, which leads to a lessening of competition.

Registration of attorneys: criteria of independence

11. Second, pursuant to Art. 8 FMAA, an attorney must be 'independent' in order to be entered in the cantonal register. The Comco advocates the interpretation of the notion of independence in the light of the Federal Supreme Court case law (see above).

Applicability of rules of professional conduct to non-registered attorneys.

12. The Comco also questioned the applicability of rules of professional conduct to non-registered attorneys. These rules of professional conduct are the correlate of the rights of audience's monopoly. According to the Comco, these rules should not be extended to attorneys who are not practicing before courts. Whereas the forensic area is regulated, legal advice is not. If a client would like to hire an attorney who is subject to these rules, nothing prevents him to do so.

E. Assessment of the effectiveness of the agency's contribution

13. In conclusion, the notarial profession is still exempt from competition rules in Switzerland, and as a result, is very well-protected. To assess the contribution of the competition agency in the attorneys area is still too early since most of the advocacies were issued in 2002 and the cantonal legislations are still in the consultation phase.

6.4. US FEDERAL TRADE COMMISSION AND DEPARTMENT OF JUSTICE

ADVOCACY AND THE LEGAL PROFESSIONS

Professions in the United States are often subject to state laws and regulations specifying who may enter the profession and what types of minimal competency requirements must be satisfied before the individual can receive a license. The legal profession is no exception. The FTC and Department of Justice Antitrust Division have had a longstanding interest in assessing the impact of such restrictions on competition.

Unauthorized Practice of Law

State statutes and regulations defining “unauthorized practice of law” (UPL) are key impediments that prevent non-lawyers from competing with lawyers in a wide variety of services. UPL statutes and regulations may be justified when excluding non-lawyers from offering a particular service advances an important consumer protection objective and the benefits to consumers outweigh the harms created by the reduction in competition. However, state UPL provisions can also prohibit non-lawyers from offering professional services that are not legal in nature (such as performing real estate closings without rendering legal advice) or from providing certain types of services that may nominally be legal services, but that some non-lawyer professionals are equally qualified to provide (such as tax advice, advice to tenants by tenants associations and to home buyers by realtors about what the state’s laws require, estate planning, the provision of legal information but not advice by trained lay people, the negotiation of agreements that could have a legal effect, the completion of purchase and sale agreements by real estate agents, and various forms of compliance training for corporate employees.)

Since 1996, the FTC and DOJ have jointly authored a series of advocacy letters opposing laws, regulations, and other proposals that would broaden the definition of “unauthorized practice of law” in ways that would foreclose competition from other professionals in rendering particular services. In real estate, for example, a number of states either require or are considering requiring the presence of an attorney at all residential real estate closings – sometimes even including refinancings of existing mortgages, where no real estate changes hands. Following a 1996 FTC-DOJ letter to the Virginia State Bar and Virginia Supreme Court opposing such a restriction, the Virginia legislature enacted a law permitting non-lawyers to conduct real estate closings. (<http://www.ftc.gov/be/v960015.htm>, <http://www.usdoj.gov/atr/public/comments/vauplltr.htm> and <http://www.ftc.gov/be/advofile.htm>, <http://www.usdoj.gov/atr/public/comments/3967.htm> .) The Supreme Court of Kentucky is considering a proposed rule that would bar lay real estate closings as the unauthorized practice of law; the Department of Justice filed an *amicus curiae brief* with the Court urging it to reject the rule in 2000 (<http://www.usdoj.gov/atr/cases/f4400/4491.htm>). More recently, the North Carolina Bar convened a special committee on residential real estate closings to reconsider that state’s prohibition on non-attorney closings in light of issues raised in a joint DOJ-FTC letter sent in December 2001. (<http://www.ftc.gov/be/V020006.htm>; <http://www.2002/07/non-attorneyinvolvement.pdf>) FTC and DOJ also urged the Rhode Island legislature to reject a bill that would have prohibited non-attorney closings; the bill was referred to a study committee and died

when the legislative session ended. (<http://www.ftc.gov/be/v020013.pdf>; and <http://www.usdoj.gov/atr/public/comments/10905.htm>)

Although FTC and DOJ advocacy efforts usually focus on policymakers, the agencies may also respond to requests for comment from private bodies that propose model statutes and regulations. In December 2002, for example, DOJ and FTC sent a joint letter to the American Bar Association's Task Force on the Model Definition of Unauthorized Practice of Law, which had drafted a definition of unauthorized practice line for consideration by state legislators and regulators. The letter suggested that the proposed definition is unnecessarily broad, citing our experience with uses of UPL to foreclose competition in real estate closings and other arenas. The letter also noted that an overly broad definition of UPL could prevent consumers from using popular software programs for writing wills and preparing other legal documents, since these programs could be considered rendering legal advice if they provide suggestions in response to information input by the customer. (<http://www.ftc.gov/opa/2002/12/lettertoaba.htm>, and <http://www.usdoj.gov/atr/public/comments/200604.htm>)

Competition within the Legal Profession

FTC advocacy also targets laws or regulations that may unnecessarily impede competition within the legal profession. The most prominent example is state regulations limiting attorney advertising.

Governments have a legitimate interest in protecting their citizens from fraudulent or misleading advertising. FTC advocacy does not question whether state governments should regulate attorney advertising. Rather, we draw a distinction between deceptive and non-deceptive advertising – thus promoting competition in the legal profession by urging state regulators to adopt an approach to attorney advertising similar to the approach the Commission takes to regulation of all advertising. FTC studies and advocacy urge policymakers to restrict attorney advertising no more than is necessary to prevent deception.

The FTC staff's most recent advocacy letter on this topic was to the Alabama Supreme Court, which solicited the FTC staff's views on some proposed revisions to its regulations governing attorney advertising. (<http://www.ftc.gov/be/v020023.pdf>) The proposed regulations prohibited references to past successes or results, testimonials, descriptions of quality, appearance of persons other than the lawyer in TV ads, or appearance of the lawyer in a setting other than his or her office, or in front of a solid color background or bookcase. Commission staff suggested that such prohibitions restrained competition more broadly than necessary and urged the Alabama Supreme Court to adopt "restrictions on advertising that are specifically tailored to prevent unfair or deceptive acts or practices."

Class Action Lawsuits

The FTC has also pursued its consumer protection mission through advocacy intended to affect the rules of civil procedure governing class action lawsuits. Largely as a result of experience with private class action lawsuits filed after the Commission files its own suit against the defendant, FTC staff noticed a number of opportunities to make the class action mechanism more responsive to consumer interests. In February 2002, the Commission recommended to the U.S. Judicial Conference, which establishes procedural rules governing class actions, several possible changes that would advance consumer interests. These include requiring private

plaintiffs' counsel in class actions to notify courts of any related actions by government agencies, requiring plaintiffs' counsel in class actions to notify government agencies involved in actions investigation of the defendant about the private class action, recommending that courts take into account related actions of government agencies when calculating attorneys' fees in private class actions, and recommending that courts make specific findings about the value of coupon settlements to consumers before approving them.

(<http://www.ftc.gov/os/2002/02/rule23letter.pdf>) The first three measures would help assure that plaintiffs receive as great a share of the class action award as possible, by prompting courts to consider how much of the award can be attributed to the actions of the private attorneys rather than government agencies. The last measure would help ensure that courts do not approve settlements in which consumers receive coupons rather than cash unless the court carefully considers whether consumers are receiving anything of value when they receive coupons.

Assessment

For several decades, FTC staff have sought to assess the effectiveness of competition advocacy through a variety of means, ranging from a formal survey of decision makers to whom advocacy materials were addressed to more informal, qualitative assessments made on a case-by-case basis. In general, competition advocacy appears to be most effective in situations where FTC staff have some additional new information to bring to the debate, such as (1) knowledge of a particular industry gained through law enforcement experience, (2) results of our own or published studies of which the participants were unaware, or (3) knowledge of the effects of similar policies in other states or localities. Advocacy also appears to be more effective when FTC staff make an effort to assess beforehand whether our involvement would likely alter the outcome; to the extent that we can focus on situations in which the FTC's views might be a decisive factor in another policymaker's decision, we can utilize limited resources more effectively.