Proposed Advisory Guidelines under the Telecommunications Competition Code 2005

Submission by Telstra Singapore Pte Limited to the Info-communications Development Authority of Singapore

6 May 2005

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EXECUTIVE SUMMARY

Telstra welcomes the initiative of the Info-communications Development Authority ("IDA") in drafting the following Advisory Guidelines under the Code of Practice for Competition in the Provision of Telecommunications Services 2005 ("Code"):

- *Advisory Guidelines Governing Abuse of Dominant Position, Unfair Methods of Competition and Agreements Involving Licensees that Unreasonable Restrict Competition ("Anti-competitive Conduct Guidelines" or "ACG"); and*

- *Advisory Guidelines Governing Petitions for Reclassification and Requests for Exemption ("Dominance Exemption Guidelines" or "DEG").*

Appropriately drafted regulatory guidelines will assist the effective operation of Singapore's telecommunications regulatory regime. Such guidelines constitute an important part of sectoral regulation in many other jurisdictions, increase regulatory transparency and provide greater certainty for all industry participants.

Telstra makes a number of recommendations in this submission, which we submit should be incorporated in the Advisory Guidelines before they are promulgated. Telstra suggests these refinements will not only benefit the industry by providing greater regulatory certainty on some critical issues, but would also assist IDA in achieving its regulatory objectives in the most efficient manner when applying the provisions of the Code.

Telstra's key points are:

A. Anti-competitive Conduct Guidelines (ACG)

Telstra suggests the following seven key amendments to the Anti-competitive Conduct Guidelines:

1. *The ACG should provide more detail on the application of the fundamentally important "unreasonably restricts competition" standard.*

2. *The ACG should confirm that Dominant Licensees are deemed to have Substantial Market Power ("SMP") under Article 8.2, but a rebuttable presumption applies following an exemption.*

3. *The ACG should address the important concept of "use" of SMP as set out in Article 8.2, thereby reducing uncertainty in differentiating legitimate from illegitimate conduct.*

4. *The ACG should include the concept of "refusal to supply" in relation to potential breaches of Article 8.2 (abuse of market power).*

5. *The ACG should refer to imputation testing when analysing whether the wholesale-retail price margin is sufficient under Article 8.2.1.2 (price squeezes).*

6. *The ACG should apply the principles of Article 8.2.2.1 (discrimination) to internal vertically integrated operations, not just structurally separated operations.*

7. *The ACG should not qualify Article 8.2.1.3 (cross-subsidisation) by a requirement of "predatory pricing", particularly as this is not a requirement of the Code.*

B. Dominance Exemption Guidelines (DEG)

Telstra suggests the following five key amendments to the Dominance Exemption Guidelines:

1. *The DEG should isolate Article 8.2 (abuse of dominance) from full exemption, and instead rather apply a rebuttable presumption following exemption.*

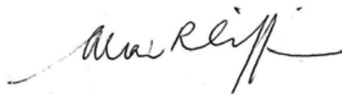
2. *The DEG should cross-reference the Competition Commission of Singapore's Guidelines on market definition, and should include more detail on functional markets.*

3. *The DEG should formally list the "verifiable data" required in support of an exemption and require this to be made publicly available where possible.*

4. *The DEG should include a more comprehensive list of factors relevant to an assessment of dominance, particularly vertical integration.*

5. *The DEG should discourage exemption-creep by adopting a holistic approach to consideration of new exemptions, including for new services.*

Telstra would be glad to discuss this submission with IDA, or provide further information, as necessary.



Telstra Singapore Pte Ltd

6 May 2005

1 GENERAL COMMENTS

1.1 Statement of Interest

Telstra Singapore Pte. Ltd ("Telstra") holds an Individual Services-Based Operator (SBO) Licence No 64387911.

Telstra Singapore Pte. Ltd. is wholly owned by Telstra Holdings Pty Limited, and is ultimately wholly owned by Telstra Corporation Limited, Australia's leading telecommunications and information services company.

In preparing this submission, Telstra Singapore Pte Ltd has drawn upon the regulatory experience of its parent company, Telstra Corporation Limited, which has operations in Australia, New Zealand, the Asia-Pacific region, and Europe, and has extensive interaction with regulators in those jurisdictions.

1.2 Initial comments

Telstra welcomes the initiative of the IDA in drafting the following Advisory Guidelines under the Code:

- Anti-competitive Conduct Guidelines; and
- Dominance Exemption Guidelines.

Appropriately drafted regulatory guidelines will assist the effective operation of Singapore's telecommunications regulatory regime. Such guidelines constitute an important part of sectoral regulation in many other jurisdictions, increase regulatory transparency and provide greater certainty for all industry participants.

Telstra makes a number of recommendations in this submission, which we submit should be incorporated in the Advisory Guidelines before they are promulgated. Telstra suggests these refinements will not only benefit the industry by providing greater regulatory certainty on some critical issues, but would also assist IDA in achieving its regulatory objectives in the most efficient manner when applying the provisions of the Code.

Telstra has summarised its key points below and has further elaborated upon these points in the main body of this submission. Telstra has confined this submission to selected major concerns it has with the Advisory Guidelines.

1.3 Consistency with international best practice and Singapore Competition Law

Telstra believes that the Advisory Guidelines should be as consistent as possible with international best practice in telecommunications regulation. In this manner, IDA will be able to more easily draw upon international experience when applying the Guidelines and can ensure its decisions are backed up with the full weight of international precedent.

Telstra also recommends that IDA seek to align the Guidelines as far as possible with the Guidelines issued by the Competition Commission of Singapore in relation to the new Singapore Competition Law. Telstra notes IDA's comments in paragraphs 2.26 and 2.27

of its explanatory paper to the Code released on 18 February 2005, which explain that IDA does not intend to import provisions of the Competition Law on a "piecemeal" basis. However, IDA should still use its best endeavours to ensure that there is a high level of consistency between the Advisory Guidelines and the Competition Law in respect of competition measures. In this manner, IDA can benefit from the development of precedents in other industries in Singapore as the Singapore Competition Law is applied.

2 SEVEN KEY REFINEMENTS ARE REQUIRED TO THE PROPOSED ANTI-COMPETITIVE CONDUCT GUIDELINES (ACG)

Telstra recommends that IDA make the following seven key refinements to the Anti-competitive Conduct Guidelines before they are formally promulgated:

1. *The ACG should contain considerably more detail on the application of the fundamentally important "unreasonably restricts competition" standard.*
2. *The ACG should confirm that Dominant Licensees are deemed to have Substantial Market Power (SMP) under Article 8.2, but a rebuttable presumption applies following an exemption.*
3. *The ACG should address the important concept of "use" of SMP set out in Article 8.2, avoiding uncertainty in differentiating legitimate from illegitimate conduct.*
4. *The ACG should include the concept of "refusal to supply" in relation to potential breaches of Article 8.2 (abuse of market power).*
5. *The ACG should refer to imputation testing when analysing whether the wholesale-retail price margin is sufficient under Article 8.2.1.2 (price squeezes).*
6. *The ACG should apply the principles of Article 8.2.2.1 (discrimination) to internal vertically integrated operations, not just structurally separated operations.*
7. *The ACG should not qualify Article 8.2.1.3 (cross-subsidisation) by a requirement of "predatory pricing", particularly as this is not a requirement of the Code.*

In the interests of brevity, Telstra has confined its submission only to these top seven issues. Telstra believes these issues are the most significant issues with the ACG and requests that each issue is carefully considered and appropriately addressed by IDA.

Telstra has elaborated on each of these issues in further detail below.

2.1 The ACG should contain considerably more detail on the application of the fundamentally important "unreasonably restricts competition" standard

Telstra notes that the "unreasonably restricts competition" standard is fundamental to the drafting of the anti-competitive conduct provisions in Articles 8 and 9 of the Code.

The standard underpins the obligation in each of the key prohibitions in Articles 8.2 (abuse of market power) and 8.3 (anti-competitive preferences) as well as Article 9 (concerted conduct).

However, IDA has provided little guidance in relation to the methodology it will apply in order to determine whether particular conduct is, as a matter of law, "likely to unreasonably restrict competition" ("URC Standard").

Telstra suggests that a greater level of detail is required in the ACG given the critical importance of the interpretation of the URC Standard to the effective application of the competition regime. Insufficient detail on this key point risks undermining regulatory certainty and will not enable market participants to properly differentiate anti-competitive conduct from legitimate fierce competition.

Telstra recommends that the IDA follow international best practice on these issues, adopting the methodology used by regulators in other jurisdictions. Telstra suggests, for example, that IDA may wish to examine for suitability the methodology used by the Australian Competition & Consumer Commission ("ACCC") or the New Zealand Commerce Commission ("NZCC") and the respective courts of those jurisdictions in determining the likely impact of particularly conduct on competition in a particular market. Other regulators and judicial institutions around the world use variations of that approach.

Under the ACCC approach, the ACCC will first predict the future likely level of competition that would prevail if the particular alleged anti-competitive conduct continues (i.e., the "factual"). The ACCC will next predict the level of competition that would prevail if the conduct did not continue (i.e., a hypothetical future situation, known as the "counterfactual"). The ACCC will then compare both situations and assess whether the factual would lead to a material reduction in the level of competition relative to the counterfactual such that the conduct should be prohibited.

This "future counterfactual analysis" has been used in Australia and New Zealand for well over two decades and provides a principled, rigorous and robust basis for regulatory decision-making. This approach is particularly important in telecommunications law given the significant adverse impact of regulatory error on dynamic markets and the high level of complexity of factual situations. Such an approach would ensure that IDA's analysis was more rigorous, defensible (including on appeal), and underpinned by a clear methodology consistent with international best practice.

Related to these issues, but equally important, Telstra suggests that the relationship between the general prohibition in Article 8.2 and the specific examples in Articles 8.2.1 and 8.2.2 is expressly clarified in the ACG. At present, it is not clear whether the specific examples are self-contained prohibitions, or whether it is still necessary for the requirements of the general prohibition to be established, hence requiring evidence that the conduct would "unreasonably restrict competition". Telstra assumes that the former was intended and suggests this should be confirmed.

2.2 The ACG should confirm that Dominant Licensees are deemed to have SMP under Article 8.2, but a rebuttable presumption applies following an exemption

Telstra notes that the policy intent behind the Singapore regime, as expressly recognised by IDA, is that: "As competition develops, IDA anticipates that it will be able to reduce the level of ex ante regulation, and place greater reliance on ex post enforcement". In this manner, ex ante sectoral regulation will be gradually replaced with a greater reliance on ex post enforcement via generic competition law.

In recognition of this, IDA expressly commented in paragraph 2.6 of the DEG:

> *"IDA will give special scrutiny to Requests by a Dominant Licensee that seek exemption from the prohibitions, contained in Section 8.2 of the Code, against abusing its dominant position. These prohibitions, which are derived from the general principles of competition law as developed in other jurisdictions, generally do not impose ex ante obligations on a Dominant Licensee. Rather, they provide an effective means of enforcement in the event a Dominant Licensee abuses its dominant position. Thus, to the extent that a Dominant Licensee retains, or has any reasonable possibility of regaining Significant Market Power in a market, IDA generally will conclude that retaining these prohibitions is necessary to deter anti-competitive conduct".*

In light of these comments by IDA, Telstra is particularly concerned by two issues associated with the drafting of paragraph 3.2 of the ACG:

- *First, Telstra is concerned by IDA's suggestion in paragraph 3.2(d) of the ACG that Dominant Licensees may not necessarily be subject to Article 8.2 (abuse of market power) where IDA has previously granted an exemption in the relevant market. Given that Singapore's generic competition law does not apply to the telecommunications sector, the effect of such an exemption from Article 8.2 will be to exempt Dominant Licensees altogether from the application of prohibitions against unilateral conduct under the competition law in Singapore in relation to telecommunications markets.*

  Telstra notes the practice in other jurisdictions is to apply an "abuse of dominance" prohibition on a case-by-case basis in particular markets based on an assessment of dominance in the particular circumstances. As identified by IDA, it remains entirely possible for a Dominant Licensee to have, or regain, Substantial Market Power in particular markets even if it has been given a historic exemption.

- *Second, Telstra is concerned by IDA's suggestion in paragraph 3.2(c)(i) that it is still necessary for IDA to establish that a Dominant Licensee has Substantial Market Power. Telstra notes that there is no requirement of SMP set out in Article 8.2 of the Code. Rather, Article 8.2 refers to Dominant Licensee status as the relevant threshold for the application of the section. In this manner, Telstra believes it is intended that SMP be automatically deemed as a result of Dominant Licensee status without any need for IDA to establish Substantial Market Power. Such an approach would also have the advantage of increasing regulatory efficiency enabling IDA to achieve its regulatory objectives in a less burdensome manner.*

Given these issues, Telstra believes IDA should take steps within the Guidelines to confirm how Article 8.2 applies, as follows:

- ***Where a Dominant Licensee has <u>not</u> been granted an exemption in a particular market, that Dominant Licensee is automatically deemed to have SMP for the purposes of Article 8.2. This approach is consistent with the wording of the Article 8.2 of the Code, which applies by virtue of the Dominant Licensee's status as a "Dominant Licensee" rather than because the Dominant Licensee has SMP.***

- ***Where a Dominant Licensee <u>has</u> been granted an exemption from Dominant Licensee status in relation to a particular market, the Dominant Licensee should be presumed <u>not</u> to have SMP in that particular market. However, this presumption should remain fully rebuttable. IDA should still retain the ability to determine that the Dominant Licensee has SMP if there is sufficient evidence available at the time to establish this, particularly if circumstances change or new evidence comes to light in relation to particular conduct.***

Telstra also notes that such an approach would be more consistent with the Singapore Government's obligations under the WTO Regulatory Reference Paper and the Singapore-Australia Free Trade Agreement ("SAFTA") as follows:

- ***Under the WTO Regulatory Reference Paper (paragraph 1.1), the Singapore Government is required to maintain appropriate measures "for the purpose of preventing suppliers who, alone or together, are a major supplier from engaging in or continuing anti-competitive practices". In this case, SingTel is clearly a major supplier.***

- ***Under SAFTA (Article 7.1), the Singapore Government is required to maintain appropriate measures "for the purpose of preventing suppliers of public telecommunications networks or services in its territory from engaging in or continuing anti-competitive practices. The anti-competitive practices referred to in Article 7.1 shall be defined in each Party's sectoral or generic competition regime, as the case may be, and shall include... misuse of market power".***

2.3. The ACG should address the important concept of "use" of SMP set out in Article 8.2, avoiding uncertainty in differentiating legitimate from illegitimate conduct

Telstra notes that the ACG does not address the concept of "use" of a dominant position as currently expressly drafted into Article 8.2, notwithstanding the fundamental importance of this term in abuse of market power provisions as a means of differentiating legitimate from illegitimate conduct.

The concept of "use" of a dominant position refers to a firm taking action that is causally derived from the additional market power that is possesses, hence constituting an "abuse". This causation is typically assessed by asking whether a hypothetical firm without market power (i.e. in a competitive market) in the same circumstances would also have undertaken the same conduct. In essence, the concept of "use" provides the basis for a causation test to assess whether a firm's conduct is consistent with the conduct of a firm in a competitive market, or whether it has arisen because the firm has abused its position of dominance. There is extensive case law around the world on these issues under a variety of different guises, including in Australia (the relevant concept is "taking advantage") and New Zealand (the relevant concept is "use").

In this manner, Telstra suggests that an appropriate, more detailed and more robust methodology that IDA could use to differentiate anti-competitive conduct from legitimate competitive conduct under Article 8.2 would be for IDA to ask itself the following questions:

- *Does the Dominant Licensee have SMP? (Under the approach identified above, SMP would be deemed if there were no exemption given to the Dominant Licensee for the relevant market. However, if an exemption had been given, a rebuttable presumption of no SMP would apply to the Dominant Licensee, such presumption discharged by evidence of SMP)*

- *Has the Dominant Licensee "used" its position? (Under the approach identified above, the relevant test would be whether or not the Dominant Licensee's conduct was consistent with the conduct of a hypothetical firm in the same situation without SMP, hence operating in a competitive market)*

- *Was the conduct likely to "unreasonably restrict competition"? (Under the approach identified above, the relevant test would compare the "factual" and "counterfactual" scenarios to determine whether there was a material adverse impact on competition resulting from the conduct).*

Telstra notes that if this approach were adopted, IDA would then be able to refer to a range of international precedent in relation to misuse of market power in telecommunications markets. In this manner, IDA would no longer be faced with the difficult task of applying and interpreting the Code in a legal vacuum (given the absence of competition law precedent in Singapore), but could increase the efficiency, accuracy and international credibility of its regulatory decisions by following settled international precedent on these issues.

2.4 The ACG should include the concept of "refusal to supply" in relation to potential breaches of Article 8.2 (abuse of market power)

Telstra is concerned that the ACG does not mention the possibility that "refusal to supply" could breach Article 8.2 of the Code. Telstra notes that the concept of a "refusal to supply" is fundamental to the application of "abuse of dominance" provisions in a telecommunications regulatory context given the very high degree of vertical integration in telecommunications markets.

A "refusal to supply" scenario usually arises where an incumbent, such as SingTel, with control over key upstream resources is competing in downstream markets with the same entities that are seeking access to those upstream resources. In such circumstances, the vertically integrated entity has a clear incentive to resist, delay and refuse access to the upstream resource, thereby delaying market entry by competitors in downstream markets.

The concept of a "refusal to supply" sets out clear regulatory parameters around such conduct, testing whether the refusal to provide access is legitimate or illegitimate. Under an "abuse of dominance" provision, the vertically-integrated firm is usually obliged by law to supply wholesale services to its competitors in circumstances where such supply is profitable, the firm has no other legitimate business justification (such as technical impossibility) why it cannot supply, and a failure to supply would materially adversely affect competition in downstream markets.

2.5 The ACG should refer to imputation testing when analysing whether the wholesale-retail price margin is sufficient under Article 8.2.1.2 (price squeezes)

Telstra recommends that paragraph 3.2.1.2(d) of the ACG is amended to contain greater detail in relation to the precise methodology that IDA will use to determine whether a wholesale-retail price margin is sufficient when analysing price squeeze allegations under Article 8.2.1.2 of the Code. Telstra suggests it would be useful for IDA to expressly endorse the concept of "imputation testing" in this regard, consistent with international best practice.

Imputation tests consider whether particular retail prices set by a vertically-integrated firm, such as SingTel, are greater than the price of the relevant wholesale (access) inputs faced by its competitors, plus the costs of transforming the wholesale inputs into the retail service. Imputation tests can be interpreted in two ways:

- ***first, as assessing whether the retail price set by the vertically-integrated firm is set sufficiently high above the wholesale (access) price charged by the firm to its competitors (as wholesale customers) to allow those equally efficient non-integrated competitors to profitably compete; and***

- ***second, as assessing whether the retail price is sufficiently high above wholesale (access) prices to allow the vertically-integrated firm to be at least as profitable as a result of servicing the end market as it would be if it sold the wholesale product to its rivals.***

Telstra suggests that IDA refers to material publicly available on the websites of other regulators for further information on imputation testing, as necessary. For example, the ACCC commissioned a report by NERA in January 2003 on Imputation Tests for Bundled Services which is available on the ACCC's website at:

- ***http://www.accc.gov.au/content/index.phtml/itemId/333868***

An imputation testing approach for determining the sufficiency of the wholesale-retail price margin would again ensure that IDA's approach is consistent with international best practice and that IDA's decisions are robust, principled and defensible. IDA would also greatly simplify the analytical steps it would need to take in order to reach a decision based on a price squeeze allegation.

By way of example, the World Bank and OECD in the Telecommunications Regulation Handbook suggest that price squeezing would be prevented if incumbents were formally required to give particular information to the regulator, as follows:

> ***"To prevent vertical price squeezing, a telecommunications regulator may impose a wholesale cost imputation requirement, along the lines set out in Box 5-9:***
>
> ***Box 5-9: Basic Rules***
>
> ***Dominant provider must provide evidence to the regulator that its retail prices are no lower than the sum of the following:***

A. The price it is charging competitors for the wholesale services that form part of the retail service (this price is said to be "imputed" in the cost of the dominant provider whether it actually incurs this cost or not); plus

B. The actual incremental costs (above the imputed wholesale costs) that are incurred by the dominant supplier in providing the retail service. For example, marketing, billing, etc. costs

Variations on this type of imputation approach have been used by various regulators and competition authorities. It is relatively simple to use (compared to detailed accounting separations or cost allocations)... What the imputation requirement assures is that the same cost for essential wholesale services is imputed to the dominant operator's retail services as is passed on to its competitors."

2.6 The ACG should apply the principles of Article 8.2.2.1 (discrimination) to internal vertically integrated operations, not just structurally separated operations

Telstra suggests that paragraph 3.2.2.1 of the ACG be amended to clarify that the principle of the non-discrimination obligation in Article 8.2.2.1 applies to a Dominant Licensee even if that Dominant Licensee has internally vertically-integrated operations, rather than structurally separated operations.

Owing to the reference to "Affiliate" in the second sentence of Article 8.2.2.1 of the Code, the IDA has taken the view in paragraph 3.2.2.1 of the ACG currently that non-discrimination obligations apply only as between a Licensee and its Affiliate, requiring that the Licensee and its Affiliate are legally separate entities. Such an approach creates a potentially large loophole in the application of Article 8.2.2.1 of the Code because the non-discrimination obligation would cease to have application to those Dominant Licensees that had internalised their vertical integration (i.e., aggregating different operations at different levels of vertical integration in the same legal entity). This is a narrow interpretation of the first sentence in of Article 8.2.2.1 of the Code, which should be held to go further and also address discrimination of the type contemplated in Articles 4.2.1.2(b) and 4.3 of the Code.

By way of example, as currently drafted, a Dominant Licensee could operate its wholesale operations (infrastructure services, wholesale services and resale services) in the same company as its retail operations (customer contracts, billing, customer interface), and could potentially give its retail operations preferable treatment, but would not appear to breach the ACG given that there would be no legally separate "Affiliate". This would have the undesirable consequence that dealings with Affiliates are subject to a broad anti-discrimination prohibition, but wholly internal conduct is only constrained by a limited number of specific provisions in Article 4 of the Code.

Given this, Telstra recommends that the ACG should comment that IDA intends to give broad application to Article 8.2.2.1 and similar provisions in Article 4, to the extent that the Licensee has vertically-integrated its wholesale and retail operations within one legal entity.

Telstra also suggests that the broader application of Article 8.2.2.1 it has identified above would be more consistent with the Singapore Government's obligations to the

Australian Government under the Singapore-Australia Free Trade Agreement ("SAFTA"). Article 9 of SAFTA provides as follows (emphasis added):

> *"Each Party shall ensure that major suppliers in its territory accord suppliers of public telecommunications networks or services of the other Party treatment no less favorable than such major supplier accords to itself, its subsidiaries, its affiliates, or any non-affiliated supplier of public telecommunications networks or services regarding:*
>
> *(i) availability, provisioning, rates, 8 or quality of like public telecommunications networks or services; and*
>
> *(ii) availability of technical interfaces*
>
> *where such suppliers of public telecommunications networks or services and subsidiaries, affiliates and non-affiliates of the major supplier are in like circumstances."*

2.7 The ACG should not qualify Article 8.2.1.3 (cross-subsidisation) by a requirement of "predatory pricing", particularly as this is not a requirement of the Code

As IDA recognised in paragraph 2.12 of its explanatory paper to the Code dated 18 February 2005, it is usually very difficult to prove allegations of "predatory pricing" in relation to telecommunications markets. The telecommunications industry is characterised by very high sunk infrastructure costs, but very low ongoing avoidable costs. In this manner, an incumbent has considerable scope to cut its prices so that it only covers its avoidable costs, discouraging roll-out of competitive infrastructure temporarily. The IDA's adoption of average incremental cost as its cost standard for testing for predatory pricing does not solve this problem.

The World Bank and OECD comment in their international authoritative publication "Telecommunications Regulation Handbook" (at page 5-27):

> *"Predatory pricing is a particularly difficult type of conduct to prove in the telecommunications industry. As previously discussed, the industry is characterised by substantial joint and common costs which are difficult to assign to particular services. The economic tests used to determine predatory pricing, such as Average Variable Costs and Long Run Incremental Costs are difficult to apply to many types of telecommunications prices".*

In addition to the substantial existing difficulties in evidencing predatory pricing in the telecommunications industry, IDA has adopted a narrow interpretation of predatory pricing in the ACG, by requiring the application of a "recoupment test" as used in the United States.

In the United States a "recoupment test" was adopted as an alternate approach to avoid the complexities of cost-based calculations. Most other jurisdictions, including Australia, only give the recoupment test evidential significance in recognition that it does not necessarily address all types of predation strategy by incumbents.

As a result, Telstra believes that IDA's concept of "predatory pricing" as identified in the ACG is drafted so narrowly that it is unlikely to have any meaningful practical

application. Rather, the Guidelines leave open very significant scope for Dominant Licensees to engage in predatory strategies, to the detriment of competition, without breaching the Code.

Telstra therefore urges IDA to reconsider its approach to predatory pricing in the Code and the Guidelines.

However, more importantly, Telstra is particularly concerned that IDA is proposing to extend the concept of predatory pricing to qualify another provision in the Code, namely Article 8.2.1.3 (cross-subsidisation). The result of such an extension would be to similarly reduce the scope for Article 8.2.1.3 to be applied, again rendering it so narrow in application that it would be unlikely to have any meaningful practical application. Again, this would create significant scope for SingTel to engage in cross-subsidising practices that adversely affect competition.

Telstra's concern is heightened by the fact that there is no mention in Article 8.2.1.3 of the Code of any requirement of predatory pricing. Section 8.2.1.2 of the Code instead sets out a broad prohibition against cross-subsidisation linked to an "unreasonably restrict competition" test. Consistent with the current wording of Article 8.2.1.3 of the Code, Telstra emphasises that it is not necessary for pricing to be predatory for cross-subsidisation to have an anti-competitive effect.

However, in paragraph 3.2.1.3(d)(iii) of the ACG, IDA has indicated that it will generally only consider that the "unreasonably restrict competition" test will be met where the Dominant Licensee has charged a predatory price. Telstra believes that this additional requirement is directly inconsistent with the intent and current drafting of Article 8.2.1.3 of the Code and risks making Article 8.1.2.3 of the Code so narrow in application as to be effectively meaningless.

Telstra therefore suggests that paragraph 3.2.1.3(d)(iii) of the ACG should be carefully reworded. The matters listed in that paragraph should not be linked by the word "and" so that they are exclusive and absolute. Rather, the various matters should be drafted as factors that the IDA may consider when determining the effect on competition.

3 FIVE KEY REFINEMENTS ARE REQUIRED TO THE PROPOSED DOMINANCE EXEMPTION GUIDELINES (DEG)

Telstra recommends that IDA makes the following five important refinements to the Dominance Exemption Guidelines ("DEG") before they are formally promulgated:

1. *The DEG should isolate Article 8.2 (abuse of dominance) from full exemption, and instead apply a rebuttable presumption following exemption.*

2. *The DEG should cross-reference the Singapore Competition Commission Guidelines on market definition, and include more detail on functional markets.*

3. *The DEG should formally list the "verifiable data" required in support of an exemption and require this to be made publicly available where possible.*

4. *The DEG should include a more comprehensive list of factors relevant to an assessment of dominance, particularly vertical integration.*

5. ***The DEG should discourage exemption-creep by adopting a holistic approach to consideration of new exemptions, including for new services.***

In the interests of brevity, Telstra has again confined its submission only to these top five issues. Again, Telstra believes these issues are the most significant issues with the DEG and requests that each issue is carefully considered and appropriately addressed by IDA.

Telstra has elaborated on each of these issues in further detail below.

3.1 The DEG should isolate Article 8.2 (abuse of dominance) from full exemption, and instead apply a rebuttable presumption following exemption

Telstra agrees with the reasons set out by IDA in paragraph 2.6 of the ACG as to why special treatment should be given to requests for exemption from Article 8.2 (abuse of dominance) of the Code.

Telstra refers to its earlier comments set out in section 2.2 of this submission in relation to the reasons why it would not be appropriate to entirely exempt Dominant Licensees from Article 8.2. Telstra also indicated in section 2.2 of this submission the proper relationship that should be adopted between exemptions from Dominant Licensee status and Article 8.2 (abuse of dominance).

Consistent with Telstra's earlier comments, Telstra recommends that paragraph 2.6 of the ACG is replaced with a simple statement that IDA will not grant full exemptions in relation to Article 8.2 (abuse of dominance) of the Code. Rather, the effect of an exemption in relation to Article 8.2 will be to remove the automatic deeming of SMP arising from Dominant Licensee status. Instead, a rebuttable presumption is created that Dominant Licensees that have received an exemption do not have SMP. IDA will be able to rebut this presumption if evidence exists to demonstrate that the Dominant Licensee still has SMP in the relevant circumstances.

3.2 The DEG should cross-reference the Singapore Competition Commission Guidelines on market definition, and include more detail on functional markets

IDA has currently drafted some detail regarding market definition into paragraph 2.4.1 of the ACG, but this detail remains skeletal in nature. The critical analysis of the appropriate functional markets contains very little detail at all.

Telstra notes that the Competition Commission of Singapore ("CCS") is currently undertaking a consultation process in relation to its own competition guidelines. These guidelines include a specific guideline on the procedure the CCS will follow in relation to market definition ("CCS Guideline"). Telstra notes that it would greatly assist consistency between CCS and IDA if the CCS Guideline were expressly cross-referenced by IDA in paragraph 2.4.1 of the ARG. The CCS Guideline contains considerably more detail on key issues relating to product and geographic market definition, so will provide significantly greater guidance to IDA on these issues. Telstra notes IDA's comments in paragraphs 2.26 and 2.27 of its explanatory paper to the Code released on 18 February 2005. Cross-referencing of the Competition Law does not amount to "piecemeal importation", when it is done for the purposes of consistency both in the short and long term.

However, the CCS Guideline currently fails to mention functional markets. Telstra believes this is an oversight and hopes it will be corrected by CCS in the final CCS Guideline. As currently drafted, the CCS Guideline may intend to treat the concept of a "functional market" as a type of "product market". Under the CCS analysis, true wholesale (non-resale) services would exist in a distinct "wholesale product market" as the wholesale products would not be substitutable for retail products. The CCS analysis would further hold that wholesale resale services are usually in the same market as the retail service given that wholesale resale services and retail services are substitutable. IDA has taken a similar view in its Explanatory Comments to the Code on 18 February 2005 in paragraph 2.8 regarding tariffing of resale services. Telstra respectfully submits that the IDA and CCS approach of subsuming functional market considerations within a product market analysis is inappropriate for the telecommunications market, which is characterised by major suppliers with a high degree of vertical integration.

Telstra notes that functional market definition is critically important to the telecommunications industry due to the extent to which retail services require a range of wholesale infrastructure inputs, including some that may be construed as "resale" services in a product market sense. In many cases, access to those wholesale inputs is essential if competitors are to compete in retail markets. Telstra therefore proposes that, as well as referencing the CCS Guideline, IDA provides greater information on the concept of functional market definition in a telecommunications context.

Telstra believes that IDA may be able to easily draw from existing descriptions of functional market definition adopted by other regulators, such as the ACCC. For example, paragraphs 5.40 and 5.64 to 5.68 to the ACCC's Merger Guidelines identify in detail the appropriate methodology for identifying the functional dimension of a market. The Merger Guidelines are available at the following link:

- *http://www.accc.gov.au/content/index.phtml/itemId/304397*

At paragraph 5.64 of the Merger Guidelines, the ACCC comments, for example:

> *"Delineation of the relevant functional market requires identification of the vertical stages of production and/or distribution which comprise the relevant arena of competition. This involves consideration of both the efficiencies of vertical integration, commercial reality and substitution possibilities at adjacent vertical stages."*

The ACCC is one of many regulators using similar approaches, and Telstra refers to its Guidelines by way of example only. IDA may prefer to examine other jurisdictions – it will find similar principles in force.

3.3 The DEG should formally list the "verifiable data" required in support of an exemption and require this to be made publicly available where possible

At present, the DEG comments that an applicant must provide "verifiable data" in support of its petition for reclassification or request for exemption. In some cases, the type of verifiable data is expressly identified in the DEG. In other cases, the applicant is left to deduce what kind of verifiable data should be supplied.

Telstra believes that the absence of a clear list in the DEG specifying what information must be provided will create a risk that insufficient data will be provided by applicants, or that applicants will be highly selective in the information they provide.

Telstra therefore suggests that IDA creates an attachment to the DEG setting out an indicative list of all "verifiable data" that is required. In this manner, there will be greater transparency in relation to the precise information required by IDA. The industry will also have greater confidence that IDA decisions on these issues are based on complete information and not a carefully crafted selective subset of information provided by the applicant.

In circumstances where an applicant does not provide information required by this list, and has no reasonable excuse for not doing so, IDA should retain for itself the ability to reject applications on the basis that insufficient information has been provided.

Similarly, if key information provided subsequently proves to be materially incorrect or misleading, IDA should include sufficient conditions within an exemption or reclassification that IDA can immediately revoke that exemption, or reverse that reclassification, on that basis.

Telstra also suggests that it would greatly assist industry consultation if all information made available to IDA by the applicant were also made available to interested parties. In this manner, interested parties would be able to identify any inaccuracies in information provided to IDA by comparing information with their own records. Inconsistencies in information supplied by applicants could be identified to IDA, ensuring high quality decision-making.

Telstra appreciates that some information provided to IDA may be viewed as confidential - so Telstra readily concedes that not all information could be made public - but we propose that the onus should be on the applicant to clearly justify to IDA why particular information is confidential and should be excluded from wider circulation.

3.4 The DEG should include a more comprehensive list of factors relevant to an assessment of dominance, particularly vertical integration

Telstra understands that a key purpose behind the DEG is to provide greater certainty to industry participants how IDA intends to assess applications for exemption and petitions for reclassification.

A critical part of IDA's assessment concerns the factors that IDA will consider when assessing whether or not a Licensee is considered to meet the requirements of the Code.

However, the factors listed in paragraph 2.4.2 currently omit a number of key issues. These include, for example, such factors relevant to dominance as:

- *essential facilities: an incumbent firm may control access to an essential facility, providing it with the ability to exploit that control so as to impede or delay market entry by competitors. The customer access network is the most commonly recognised essential facility in the telecommunications industry. However, essential facilities may also include other resources that cannot be economically duplicated, or are inherently scarce, such as telephone numbers and radiocommunications spectrum;*

- ***natural monopoly characteristics:*** ***telephony networks have inherent natural monopoly characteristics as they usually exhibit declining costs up to the point where universal service is achieved;***

- ***legacy ownership:*** ***the incumbent may have received significant infrastructure from the Government as part of a corporatisation process, essentially debt-free. The incumbent may own a large proportion of these resources and exercise its ownership right to control access to those resources by its competitors;***

- ***network effects: network effects involve an economic externality that arises because the value of a telecommunications network increases for all subscribers the more people are connected to it. Consequently, when a new subscriber joints, other subscribers also benefit. In this manner, the owner of the largest network can offer its subscribers the greatest benefits in the form of any-to-any connectivity;***

- ***switching costs:*** ***customer switching costs may include, for example, the costs involved in churning customers between firms, including costs associated with number portability. The existence of such switching costs means that the market incumbent may have a competitive advantage due to customer inertia and customer transfer costs; and***

- ***vertical integration:*** ***vertical integration causes problems where an entity with control over upstream essential resources may be competing in downstream markets with the same entities that are seeking access to those upstream resources. In such circumstances, the vertically integrated entity has a clear incentive to resist and delay access to the upstream resource, thereby delaying market entry by competitors in downstream markets. Telstra emphasises again that this issue of vertical integration is particularly important in the telecommunications industry given the ability of a firm with market power in an upstream market to leverage that market power to benefit itself in a downstream market.***

IDA itself has also given weight to a much larger range of factors in the previous instances where it has considered dominance exemptions, hence it would be appropriate to include those previous factors into the Guidelines as well, therefore formally endorsing the previous precedent established by IDA

Telstra further suggests that it may be useful for IDA to also adopt various factors that have been identified by other regulators as a basis for assessing "dominance". Of most relevance would be the dominance criteria used by the European Commission and key European regulators, such as OFCOM. In this manner, IDA could potentially achieve its regulatory objectives in a less burdensome manner (consistent with Article 1.6.2 of the Code) by following previous precedent, rather than developing its own precedent afresh.

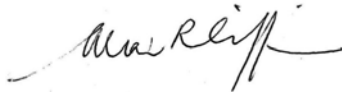
3.5 The DEG should discourage exemption-creep by adopting a holistic approach to consideration of new exemptions, including for new services

Telstra has concerns in relation to SingTel's incremental approach to exemption applications under the Code. An incremental approach risks weakening the analysis undertaken by IDA as to whether an exemption should be granted as it may be easier for SingTel to demonstrate that the effect of a particular exemption is de minimus, even through the aggregate effect of multiple exemptions is very substantial.

As Telstra understands it, a Dominant Licensee has every incentive to submit exemptions in the hope that it will receive an exemption, as it has little to lose and everything to gain by doing so.

Telstra therefore believes it is important that the Guidelines discourage exemption creep and regulatory gaming by Dominant Licensees by indicating that IDA will reconsider previous relevant exemptions it has granted to a Dominant Licensee at the same time it considers granting new exemptions. In this manner, IDA will adopt a holistic approach and will consider the aggregate effect of all exemptions when making its decision.

Telstra also notes that the Guidelines do not appear to address new technologies and services that develop over time and that may materially affect an existing exemption. In IDA's previous exemption decisions, SingTel has been required to approach IDA with a new exemption application in circumstances where a new service is developed. Telstra believes that this precedent should also be formalised in the Guidelines.



Telstra Singapore Pte Ltd

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