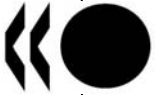


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Global Forum on Competition

ROUNDTABLE ON BRINGING COMPETITION INTO REGULATED SECTORS

Contribution from Chile

-- Session I -

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ROUNDTABLE ON BRINGING COMPETITION INTO REGULATED SECTORS

1. The evolution of the long-distance telephone service in the Telecommunications Market

1. Prior to privatisation, Chile's telephone system was dominated by two state-owned companies: Compañía de Teléfonos de Chile ("CTC"), which provided local telephony services, and Empresa Nacional de Telecomunicaciones de Chile ("ENTEL"), which provided domestic and international long-distance services. By 1989, many other companies were interested in providing long distance services; several firms, including CTC, applied to the telecommunications regulatory agency ("SUBTEL"), for operating licenses in long-distance service. Although a consensus had been reached on the need to end monopolies in long-distance services, doubts emerged about whether local telephone companies should be allowed to participate in the long-distance business. It was feared that the local telephone companies, a natural monopoly, would tend to favor their own business in long-distance services, for example, by giving its competitors poor interconnections. It was generally thought that it would be too difficult to put a regulatory scheme in place capable of preventing discrimination entirely. Three factors contributed to this belief: 1) it would be too difficult to enforce technical standards, 2) the regulatory system was not sophisticated enough, and 3) the legal system did not facilitate conflict resolution.

2. The regulators, on the other hand, were aware that vertical integration has its advantages. For example, it makes it possible for telecommunications companies to utilize existing economies of scope in providing services and for consumers to sign up with a single company for all services. Although it would be ideal for integrated companies to compete in offering a wide array of services, the nature of a natural monopoly in basic telephone services, coupled with a highly concentrated market share of these services in a single company (nearly 95 percent of Chile's subscribers were with CTC at the time) made this option difficult to achieve.

3. In June 1989, SUBTEL consulted the antitrust authorities to inquire whether entry of local telephone companies into the long-distance business would clash with the provisions of the Competition Law, especially in the case of CTC. In November of that year, the Antitrust Commission, decided that, by adopting measures and precautions set forth in the ruling, local telephone companies could provide long-distance services. These measures limited local telephone companies' long-distance participation to a multi-carrier dialing system that enabled users to select a long-distance carrier for individual calls by dialing a certain number of digits.

4. The Antitrust Commission also directed local telephone companies to provide all long-distance operators equal opportunity to interconnect with the local network, with fees access approved by SUBTEL. Moreover, the companies that became vertically integrated were required to undergo this process by means of subsidiaries chartered as publicly traded stock corporations that forced transactions between the parent company and subsidiary to emulate market conditions. Also the Antitrust Commission made it mandatory for local telephone companies to provide carriers all information related to long-distance traffic (for example, subscriber number, type of traffic, billing amount, and carrier used) and to offer the long-distance companies metering, appraisal, and billing and collection services, abiding by non discriminatory rates pre-approved by SUBTEL.

5. In response, ENTEL filed an appeal known as "petition in error"¹ with the Supreme Court, which, in May 1990, nullified the earlier resolution and sent the case back to the Antitrust Commission. In formulating its ruling, the Court said that the Antitrust Commission failed to include in its argument all relevant technical information needed to establish that, with currently available technology, it would be

possible to ensure compliance with essential conditions to establishing a competitive long-distance market. In addition, the Court ordered the Commission to carefully decide which technical conditions would guarantee fair-market conditions, including supervision of interconnection quality. Consequently, this was the central focus of the rehearing before the Antitrust Commission.

6. The rest of the telecommunications companies claimed that CTC's integration into long-distance services would make it possible for that company to extend its monopoly from local to long-distance service, despite installation of a multi-carrier dialing system. From these companies' perspective, CTC could provide different levels of quality in the interconnection, thereby adversely affecting service quality of potential long-distance competitors, since the technical, financial, and legal means to implement all required monitoring or oversight to guarantee non discrimination were not in place.² Furthermore, CTC would have incentive to transfer profits from the regulated market to the competitive market. Being the only company in direct contact with users, CTC would have a commercial advantage. Finally, having prior access to information related to long-distance service would make it possible for CTC to offer different service plans.

7. CTC argued that the Antitrust Commission did not have the legal authority to prohibit market access in the absence of an unlawful act or event to justify its intervention, since the function of the Antitrust Commission was to sanction unlawful acts classified in the Competition Law, not to decide about a market structure. It also asserted that installation of a multi-carrier dialing system would prevent non-tariff discrimination. Furthermore, it claimed that operating its long-distance service through a subsidiary subject to supervision Chilean Securities and Insurance Supervisor would be sufficient guarantee that no cross subsidies between CTC and its long-distance affiliate would occur. Lastly, CTC offered to set aside a minimum of 10 percent of the capital shares of its long-distance subsidiary for another telecommunications company, also giving it the right to appoint at least one member to the subsidiary's board of directors.

8. The Antitrust Commission issued its new ruling in April 1993.³ As a preliminary matter, the Commission addressed the issue of the scope of its authority. It maintained that, contrary to the CTC's claim, the Commission had the discretionary power to rule on the matter submitted by SUBTEL, even though the case did not involve an offence or crime as such. Thus, it rejected allegations regarding its lack of jurisdiction to establish regulations. Regarding the merit of the case, the Commission held that it was improper to divide up the telecommunications market into segments, citing that technological advancements in this sector made it difficult to differentiate between services. Nevertheless, it warned that vertical integration posed a risk to fair competition, which made it necessary to establish an efficient, strictly controlled, regulatory framework with drastic sanctions for offenders. In its ruling, the Commission reiterated the measures that must be adopted before deregulating the long-distance market, giving the government 18 months in which to implement them⁴. In addition, SUBTEL was ordered to regulate direct connection of users to long-distance companies.⁵

9. Law 19,302, which establish the way for deregulating long-distance services, was approved in March 1994. This law encompassed all of the requirements imposed by the Antitrust Commission and included a constraint on participation of all companies in the long-distance market over the subsequent five years. These constraints were most stringent for carriers affiliated with local phone companies. The multi-carrier system became operational in October 1994. Deregulation of the long-distance market met expectations. New firms, including CTC-Mundo - CTC's subsidiary - entered into the long-distance service market. The volume of international calls handled by ENTEL, which had held a monopoly position until 1994, dropped to less than 41 percent of total volume by 1995, and its market share in this sector continued to decrease (Table 1). ENTEL's market share drop was even more dramatic in domestic long-distance calls where it fall to 37.4% by the end of 1994.⁶

Table 1: Companies' Participation in the Long-distance Service Market
(by minute transferred)

Company	Domestic Traffic (%)		International Traffic (%)	
	2003	1994	2003	1995
ENTEL	35.5	37.4	34.0	40.5
CTC-Mundo	38.2	28.9	19.6	20.7
Chilesat ⁷	19.1	21.9	18.5	19.4
Others	7.2	11.8	27.9	19.4

Source: SUBTEL

10. Long-distance rates dropped dramatically, as evidenced by the change in the cost of a one-minute phone call from Chile to the U.S., a route that represents 42 percent of total international traffic. During peak hours, the regulated rate had been US\$2.40 per minute, while today, the same call costs less than US\$0.3 per minute.⁸ The rates' drop causes a strong increase in traffic, indeed between 1994 and 1996, the international long-distance traffic grew a 116% and the domestic one and 165%.

11. Giving subscribers the ability to select a particular carrier by simply dialing two digits for each call made it easier for competition to thrive in this sector. In countries with less competition than Chile, multi-carrier systems require that users call through the company with which they have a service contract. This explains why the Antitrust Commission prohibited cutting off multi-dialing service to subscribers under a service contract. In 1996, CTC-Mundo offered appealing discounts to any users who requested that CTC, the parent company, disconnect the multi-carrier dialing, leaving active-service contract dialing through that company. The Antitrust Commission admonished CTC-Mundo to discontinue the offer. Today, there are 26 carriers operating using the multi-carrier dialing system.

NOTES

1. The parties affected by the decisions of the Antitrust Commission usually file with the Supreme Court a special appeal, known as a “petition in error,” which relates to the procedural, rather than meritorious, aspects of the original Commission proceedings. If the appeal is accepted, the Court requires the Commission to amend the “mistake or abuse” committed when the Commission issued the decision being challenged. Thus, using petition in error, the substance of a decision can be modified, even though, in principle, this was not permitted.
2. These companies argued that quality discrimination does not have to be ongoing to be effective.
3. Some companies filed an appeal against the decision of the Antitrust Commission with the Supreme Court, alleging that the Commission was not empowered to regulate situations that are properly governed by law. In its 1994 decision, the Court denied the appeal, declaring that the Antitrust Commission has the power to issue resolutions of a general nature to which private parties must adhere.
4. Perhaps the only difference between Resolutions of 1989 and 1993 is that the latter allowed service contracts and multi-dial service to coexist, while the former only accepted the dialing multi-carrier.
5. Direct connections are those that bypass the network of local companies, which, prior to that time, had not been permitted.
6. However, long-distance service is still concentrated, largely because only three companies (CTC-Mundo, ENTEL, and Telex Chile) had fiber optic networks that covered the entire country, making it necessary for other carriers to lease use of this network from these companies.
7. Former Telex-Chile
8. This dramatic price decrease can be attributed, in part, to technological changes and elimination of cross subsidies.