



**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS  
COMPETITION COMMITTEE**

**DAF/COMP/WP2/WD(2005)54  
For Official Use**

**Working Party No. 2 on Competition and Regulation**

**ROUNDTABLE ON THE IMPACT OF SUBSTITUTE SERVICE ON REGULATION**

**---Turkey---**

**30 May 2005**

*The attached document is submitted by the delegation of Turkey to the Working Party No. 2 of the Competition Committee FOR DISCUSSION under Item VII of the agenda at its forthcoming meeting on 30 May 2005.*

**JT00185134**

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### **Competition From Substitute Services in Regulated Industries**

1. As services in regulated sectors have significant importance because of their contribution to whole economy, emergence of alternatives and competition from substitute services, at least on the margin, on these regulated services presents new opportunities. However, the emergence of substitute services also brings challenges for the regulatory frameworks. Because of these opportunities and challenges brought about by substitute services, there has been a need for the review of existing regulatory frameworks in regulated industries, particularly in electronic communications industry, in many jurisdictions.

2. Given this background, this paper will provide a general overview about the development of substitute services in regulated industries in Turkey and an analysis of broadband Internet services over Cable TV (CATV) as a substitute service.

3. Generally, it can be stated that while substitute services have not yet emerged as a competitive alternative in some industries, some other industries face to competition from substitute services.

4. In that context, for example, the share of railways is 3,8% for freight and 2,6 for passenger transportation in Turkey. These figures indicate that rail services are not a viable substitute for different transportation modes. On the other hand, air transport has become a substitute for bus services in some national routes with the increasing competition in the air transport industry achieved by recent liberalisation efforts which led to the fact that some bus service companies announced discounts in their prices because of the competition from the air transportation. A similar example may be in the petroleum industry. Because of the regulatory asymmetry stemming from different tax regime, Liquid Petroleum Gas (LPG) has partially become a substitute for diesel oil and benzene.

5. However, as it is the case around the world, telecommunications industry presents great potential for the emergence of substitute services in Turkey. Liberalisation efforts and technological developments, especially digitalisation, by paving the way for the provision of new and traditional services over different networks, lead to the emergence of substitute services in this sector. These developments require regulators to depart from technology-based regulation to technology neutral regulation. In this context, the emergence of new services over the CATV such as broadband Internet services, voice services and multimedia services, has the potential to become a substitute for services provided over Public Switched Telephone Network (PSTN). However, the emergence of substitute services over the CATV has been delayed, as both infrastructures has been owned by Turk Telecom, state-owned incumbent fixed-line operator, until recently. Therefore, ownership of the CATV and practices of Turk Telecom related to the operation of the CATV have been subject to the competition law enforcement as will be described in detail below.

#### **The CATV as a Substitute for the PSTN in the Broadband Access Services**

6. Turk Telecom has retained a legal monopoly over voice services over the PSTN and related infrastructure until the end of 2003 in Turkey. As no licence has been granted to any other operator until now, Turk Telecom has also owned de facto monopoly over the CATV network. Turk Telecom has rolled out and operated the CATV network in revenue sharing model with sub-contractors assigned in different regions. In August 2004, the CATV network has reached about 2,5 millions households and has around 1 million subscribers. Compared to the PSTN, which has around 19 million subscribers, the CATV, despite its potential for growth, is a smaller network than the PSTN. However, the CATV has been rolled out mainly in big cities that its customer could demand new services over this network.

7. Current regulatory framework in Turkey is mainly based on the legislation adopted in 2000, which amended the old statutes and established an autonomous regulator (Telecommunication Authority "TA"). In addition to the sector-specific legislation, Act on the Protection of Competition No.4054 (the

Competition Act () is implemented by the Turkish Competition Authority (TCA) in this sector as a part of the regulatory framework.

8. With the advent of Internet, the CATV network, together with the PSTN, has become one of the main infrastructures to provide Internet access services particularly the broadband Internet access services. While access to the PSTN by Internet Service Providers (ISPs) is regulated, there has not been any regulation about access to the CATV to provide Internet access services. So, Turk Telecom, as the owner of both networks, refused to grant access to its rival ISPs to the CATV network. Turk Telecom first began to provide this service over the CATV network and had approximately 43,000 subscribers in August 2004. But later, it focused on the provision of ADSL based services over the PSTN. However, after it focused on ADSL, Turk Telecom continued to refuse granting access to any ISP other than its Internet branch to the CATV network and did not invest in the network to make more network nodes available for the provision of broadband Internet services. The TA has not adopted any effective regulation in this process to force Turk Telecom to open up its CATV network to ISPs. Therefore, despite its potential, broadband Internet services over the CATV network could not become a substitute for ADSL based Internet services in Turkey.

9. The TA regulates the broadband access services over the PSTN, however it does not regulate broadband access services over the CATV. So, while ISPs can have access to the PSTN network to provide broadband Internet services, they cannot seek access to the CATV network. The main aim of the regulation is to ensure the provision of services to the end users in a standard quality and at reasonable prices, and competition between ISPs in the provision of broadband Internet services. Presence of substitute service over the CATV would promote this objective. The substitute service also does not undermine any objective of the regulation.

10. The TA, after liberalisation, is in the process of adopting and enforcing necessary secondary legislation especially regarding the licensing and access regime. The TA also plans to adopt a technology neutral regulation by defining markets in accordance with competition law principles following the regulatory model of the EU, which has been adopted in the New Regulatory Framework. In this context, although secondary legislation has been adopted recently about the licensing of new CATV operators, no license has been granted to any operator so far. Authorisation of new operators will, in the long run, lead to increase in substitute services from the CATV. However, it can be stated that there is not any immediate policy action to ensure a level playing field between broadband Internet services over the CATV and the PSTN.

### **Competition Law Enforcement**

11. Issues relating to the CATV network have been subject to the competition law enforcement in two ways. First, the TCA investigated Turk Telecom's refusal to grant access to ISPs to the CATV network. Second, in the privatisation process of the Turk Telecom, the TCA adopted an Opinion in order to forward to Privatisation Administration before the bidding process, which was proposing, inter alia, the structural separation of the CATV network from Turk Telecom.

12. Cable Modem Services Investigation was about Turk Telecom's refusal to grant access to its CATV infrastructure. As mentioned above, Turk Telecom has owned both CATV network and PSTN that are essential infrastructures for Internet Service Providers (ISPs) to provide broadband Internet access services. Turk Telecom first began to market its broadband Internet services over its CATV network by refusing other ISPs who demanded access to that network. When Cable Modem Services investigation was initiated, as the PSTN was not available for the provision of broadband Internet access services (ADSL Internet services), Turk Telecom was the sole provider of broadband Internet access services. In the investigation process, Turk Telecom began to provide ADSL based Internet services.

13. Considering these facts, Turk Telecom was accused of monopolising Internet access services over the CATV network and restricting production, marketing or technical development thereby causing a disadvantage for the consumers. The TCA concluded that broadband Internet services over the CATV and ADSL were in the same market, Turk Telecom possessed a dominant position in this market and Turk Telecom abused its dominant position by refusing other ISPs to access to the CATV network. For the remedy, the TCA ordered Turk Telecom to open its CATV network to rival ISPs.

14. This case indicates that incumbent operators can prevent emergence and development of substitute services by engaging in exclusionary practices like denying access to essential infrastructures.

15. Second, the TCA's Opinion in the privatisation process about the separation of the CATV network from Turk Telecom mainly reflects the need for developing competition between services provided over competing infrastructures.

16. The TCA issued a Communiqué in order to establish a procedure of cooperation between the TCA and Privatisation Administration regarding privatisation transactions. This Communiqué sets out a separate advance notification requirement for privatisation transactions, which are exceeding the thresholds specified. This requirement aims that Turkish Competition Board can provide its views on the proper method of structuring sale of the privatisation assets before the tender process. Thus, the Board has two opportunities to influence the outcome of the privatisation, one at the time the tender is devised, and again when a particular firm is identified as the acquirer.

17. In the privatisation of Turk Telecom, the TCA adopted an Opinion that addressed the CATV among a number of other issues. In this Opinion, the TCA, by highlighting the importance of competition between alternative networks, mentioned that the CATV network presents potential for the provision of competing services to the services provided over the PSTN. The TCA also stated that access services that are essential for service providers, especially for ISPs, provided over both networks are in the same market especially in the case of broadband services considering that retail services provided over both networks are interchangeable for end users. Following these assessments, the TCA concluded that even access to an infrastructure is subject to tight rules, it cannot be sufficient for ensuring targeted competition in the absence of competition between these infrastructures.

18. Considering assessments mentioned above, the TCA concluded among others that performing privatisation in the line of the following would be beneficial for ensuring the creation of a more competitive market structure:

“The infrastructure of cable TV be rendered a separate legal personality together with all rights related to the ownership and operation of this infrastructure, such that it shall be completed within the period of one year at the latest, following the transfer transaction of the Turk Telekom A.Ş, and the control of this legal personality be transferred.”

19. Following this Opinion, Privatisation Administration prepared a privatisation tender that the CATV network would not be included in the sale of Turk Telecom. Recently, a legislation that transfers the CATV from Turk Telecom to Turksat, a state owned satellite operator, has been adopted.

20. With this Opinion, the TCA aimed to ensure a market structure that ownership of the CATV network and PSTN is separated. With the separation and transfer of CATV network from Turk Telecom, it is expected that competition in the services provided over these networks, especially in the broadband Internet services, could be created and increased.