

Telecoms Infotech Forum

Briefing paper

Regulating convergence

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I. Good regulations or a good regulator?

Around the world the issues being thrown up by convergence between the communication industries (principally broadcasting and telecommunications, but also the computer and networking sectors) are being debated, as is the best policy platform for regulating convergence.

In the US the Telecommunications Act of 1996 opened the doors to telecommunication companies (telcos), cable TV companies and information network service providers entering each other's markets. Both the European Union and the United Kingdom initiated formal public consultation processes in 1998. Hong Kong launched its own convergence debate via simultaneous policy reviews of the telecommunication and broadcasting sectors in September 1998. These debates have several themes in common, which should not be surprising for not only are the technological drivers of convergence broadly the same, so too is the evolution of the policy debate. The issues being thrown up by the convergence of the communication industries fit into a broader movement with its antecedents in the mid-1980s: that of deregulation and the pursuit of the level playing field.

The concept of deregulation originally appeared deceptively simple: the lifting or abolishing of government regulations in order to allow markets to work more freely, as posited by classical capitalist economic theory. Proponents believed that government regulations distorted the efficient working of market. But in contrast to this "deceptively simple" presentation, deregulation turned out to be extremely complex. Indeed deregulation was unable to take place without the creation of new regulations to replace the old. By the mid-1990s, deregulation had become re-regulation.

Technological and commercial convergence compounded this complexity, and the pursuit of the "level playing field" evolved into overarching pro-competitive policies and "economic regulation". How best to achieve these objectives?

Evolution or revolution?

A central issue which the debates worldwide have focused upon is whether the challenges of convergence are best handled by evolution or revolution—whether a new regulatory structure should be built on the back of existing laws and regulatory bodies, or whether entire new regulatory infrastructures are required.

In most jurisdictions, discussions are largely pointing towards the acceptance and promotion of evolutionary change. The main reason for this is the uncertainty that lies ahead. One thing on which almost everyone agrees is that while the digital revolution may be well under way, its implications will take years to play out. Faced with such a future, constructing an entirely new regulatory infrastructure may prove to be not merely ambitious, but hazardous, even if some feel that in certain areas, such as the Internet and E-commerce, there may be little choice.

For many involved in the debates, caution appears to be the best way to handle what is clearly a transition period, if only on the grounds of

providing precedent, especially as broadcasters begin entering the world of telecommunications, and the telcos begin involving themselves in content.

Evolutionary change is also a means of avoiding what would otherwise be a drafting nightmare if legislators in the European Union or the United States were required to draw up new rules from scratch amidst the competing claims of many hundreds of large companies, organizations and institutions. But would the same hold true for national jurisdictions, such as Australia or the UK? And what of even smaller geographical and economic units, such as Hong Kong? Given that convergence is bringing enormous change, will those locations which can prove most flexible be the ones who are best able to take advantage of the opportunities that present themselves?

If what is needed are regulations which can only be provisional, perhaps the current focus should in fact be upon excellent regulators—individuals or bodies with the vision and powers to be able to adjust regulation almost on the fly, and to do so in a way that would be generally perceived as fair and for the best. In many parts of the telecom world this was precisely what was adopted through the early- or mid-1990s. In a number of these cases—such as Australia, for example (see below)—once the transition period had been seen to have ended, the regulator was subsumed within a broader pro-competition body, and the industry moved towards self-regulation.

Even the best of regulators, however, do not operate in vacuum. Moreover, companies faced with regulatory uncertainty do not tend to commit large, or long-term investment as is required to develop a convergence infrastructure. So by what criteria could regulators looking to maximize flexibility set out to lay down the rules?

An intriguing prospect for Hong Kong is whether, given its size, openness and history of fast reaction to changing economic times, it could be both a testing ground for new regulatory forms and a major beneficiary from being the first to adopt them.

This briefing paper considers this question in the light of the debates taking place around the world. Section II draws out some of the main convergence themes under discussion in a few of more developed global markets (the European Union, UK and Australia). In Section III, we outline the issues facing policy-makers and industry in Hong Kong, and ask which (if any) of these outside models provide applicable approaches to Hong Kong's convergence agenda.

II. Regulatory frameworks

European Union

With national as well as corporate interests at stake, the European Union has the most complex task of any region looking to coordinate a response to convergence. Through the first half of 1998 it gathered opinions on a Green Paper on Convergence issued in December 1997, which took as its starting point three options:

1. Building on current structures.
2. Developing a separate regulatory model for new activities, which would coexist with telecommunication and broadcasting regulation.
3. Progressively introducing a new regulatory model to cover all existing and new services.

Among the general themes that arose from the submissions was a strong preference for an evolutionary approach to change with the goal of creating a predictable regulatory framework that would encourage investment.

Two areas of discussion came to the fore:

- Where should competition be applied and to what extent should it be balanced against sector specific rules.
- What new regulations, if any, should be applied to on-line services, especially the Internet.

Competition was largely regarded as the way to regulate content, especially for on-line services and publishing. The licensing regimes that exist across Europe were not seen as a barrier to entry, but nor was there much support for views suggesting licenses should be anything but the exception in IT and publishing.

To facilitate competition, the general consensus was that future regulation should aim at being technology and platform-neutral. At the same time, competition rules would have to be applied rigorously in order to prevent existing network operators exploiting their positions unfairly. The main concerns expressed here were by broadcasters worried about telecom companies using cross-subsidies and telecom and broadcasting companies worried about commercial threats from public broadcasters.

To a far greater extent than anywhere else in the world, the views backed roles for regulatory structures to watch over the interests of consumers, not just from the point of view of purchasers of products but also as people who had the right to receive diverse content with a plurality of outlooks. There is a strong body of opinion that public service broadcasting should not only be maintained but should embrace the new opportunities of convergence. Moreover, for many this was seen as commendable in its own right, but partly tempered by the fact that some public service broadcasting cannot hold its position on the basis of market demand alone.

The submissions also generally maintained that while change was coming it was not likely to be overnight. In Europe, the broadcasting industry is largely expected to remain in the same form it has now, with markets determined along national and linguistic lines. Broadcasters in particular suggested that uncertainty was concentrated at the margins of their activities, and that their key business would remain largely unchanged.

Source: European Commission, www.ispo.cec.be/convergencegp/

United Kingdom

The UK is clearly opting for an evolutionary approach. While it acknowledges that convergence calls for new regulatory approaches, it believes that change is happening at a pace which can be handled through adapting existing regulatory bodies rather than starting again from scratch.

It does, however, have guidelines for handling change. In its discussion of the issue, *Regulating communications: approaching convergence in the Information Age* issued by the Department of Trade and Industry, these are outlined as:

- Greater coherence in economic regulation across all digital delivery media.
- Reassessment of the current regulatory distinctions based solely on the method of delivery to the consumer.

In the paper, the government undertakes to maintain the role of public service broadcasting as a major benchmark of quality and as a guarantee of diversity and impartiality. It also notes that the market alone provides no guarantee that expectations of plurality, diversity and impartiality can be met. Other means will be needed to ensure that programming meets these criteria.

One of the backbones of the UK's approach is reliance on a Competition Bill currently being enacted. It notes that in economic regulation, it will build "on the Competition Bill powers and progressively withdraw[...] from additional regulation down to the minimum needed to deal with such issues as bottleneck control, interoperability and universal access".

Beyond this it plans to build regulation based on categories of service reflecting differing consumer expectations.

To this end, as well as enacting the Competition Bill, the government is also ending restrictions barring telecommunication operators from transmitting entertainment and pushing its main regulators—the Office of Fair Trading, OFTEL and ITC to cooperate and collaborate more closely.

The government also intends to introduce a Secure Electronic Commerce Bill to legalize digital signatures and establish encryption standards.

Source: Department of Trade and Industry, www.dti.gov.uk/converg/

Australia

Australia's experience of convergence is of particular interest because of its early acceptance of evolutionary as opposed to revolutionary change in its policy towards convergence.

At the beginning of the 1990s it was widely believed that existing legislation covering telecommunications, broadcasting and other relevant areas would be merged into an over-arching Communications Act. This approach was abandoned in 1995 with a decision to make state utilities answerable to general competition legislation. As a consequence, the sectors covered by convergence, although unified at a government level under the Minister for Communications, the Information Economy and the Arts, each has its own piece of legislation and regulator.

Broadcasting is governed by the Broadcasting Services Act 1992, which is overseen and implemented by the Australian Broadcasting Authority. The Act's main thrust is aimed at regulating program standards and codes, and overseeing ownership and control of broadcasting to prevent concentration of the media in the hands of one company. It does not cover electronic information such as on-line services but draft legislation to include these areas was put forward during 1998.

The Telecommunications Act 1997, overseen by the Australian Communications Authority, specifically excludes content issues. It is focused principally on technical matters. To cover the issues thrown up by the opening of telecommunications to competition, the sector is also governed by competition legislation, namely the Trade Practices Act 1974 and its oversight by the Australian Competition and Consumer Commission, founded in 1995.

Because of the maintenance of this split between telecoms and broadcasting, on-line and related electronic services are either covered at separate points in different laws or fall into gray areas. For example backing for local content has always been present for films and broadcasting, either in the form of direct support or limits on foreign productions, but it has not yet been established for multi-media.

However, the government is also attempting to promote on-line activity with support provided to business via customs and duty-free trading on the Internet. Via its National Office of the Information Economy, set up in 1997 with around 15-20 staff, it encourages the general raising of awareness of on-line and related services in the private sector, while its On-line Council concentrates specifically on coordinating government initiatives.

Source: Media and Telecommunications Policy Group, RMIT, *The Communications Environment: Australia 1998*

III. Convergence in Hong Kong

What can Hong Kong learn from the discussions on the regulation of convergence taking place around the world? This section outlines some of the central issues facing Hong Kong's policy-makers in the light of the experiences of other countries.

1. Evolution or revolution?

Should regulations be built on the back of existing rules and bodies or is a totally new approach required?

Question marks hang over many parts of Hong Kong's current regulatory systems covering broadcasting and telecommunications. In particular, the opening to competition in both sectors continues to be, if not piecemeal, certainly not holistic. The central domain of the broadcasting sector—free-to-air broadcast—remains an oligopoly; in telecommunications only four licensees exist for the fixed-line market, and the moratorium on the provision of new licenses may well be extended for up to three years; in the Internet market, one player (Hong Kong Telecom) may well now have 70 per cent of all subscribers.

2. Sector specificity.

To what extent should broadcasting and telecoms be governed by sector specific regulations rather than falling under general provisions such as competition laws?

While the general tendency of commentators is to look to market opportunities which convergence may throw up, and thus to emphasize the role of general regulations such as competition legislation, there is a strong chance that broadcasting and telecommunications will in many respects look quite similar in a decade. If this is the case, then it needs to be asked what is wrong with existing legislation rather than what is right with proposed meta-legislation, such as a competition law.

3. What will be the impact of global access to digital media?

The death of distance, while usually applied to telephony and the falling rate of international calls, will have a far greater impact in the offering of opportunities to buy goods and services. This will be true especially for products that can be used or delivered digitally, to places where they could not be delivered before. Among the examples already available: on-line shopping, gambling and share trading. Downloadable music will follow soon, and, when the bandwidth becomes available, so will video entertainment.

Can Hong Kong afford to be sanguine about this? It perhaps has fewer problems to worry about than many other places. With few import duties and no sales tax it has far less to worry about in the tax implications of purchases made from abroad over the Internet than countries with high tariffs or sales taxes.

However, while threats to the existing structure may not be so great for Hong Kong, this does not address the issue of how Hong Kong can benefit from digital distribution and the erosion of national barriers. Specifically, as a service economy, how can the new media be exploited to make Hong Kong's services more tradeable? How can Hong Kong's competitive advantage be increased?

Convergence clearly offers new scope for Hong Kong to revitalize its video content industry, but the government faces a dilemma. Against the spirit of free trade, and against the tide of world trends, Hong Kong has banned parallel importing. There is already some evidence that consumers have lost choice and pay higher prices as a result, but without some kind of protection can local industries like film and music survive? Is there a measurable trade-off here, or should Hong Kong focus exclusively upon piracy and intellectual property issues?

4. Whose interests need protecting and promoting?

Hong Kong, despite its claim to be a full-blooded *laissez-faire* economy, is home to many interests protected from both domestic and international competition. Broadcasting and television are among these. Ironically, the opening of these sectors in the 1990s to limited competition has increased rather than decreased the number of organizations arguing for preferential treatment—usually couched in terms that they would not invest unless guaranteed protection from competition for a certain period of time. How constructive a presentation is this?

Hong Kong Telecom's IMS subsidiary owns both of Hong Kong's licenses for video-on-demand. Hong Kong Cable (formerly Wharf Cable), remains Hong Kong's only cable television company. Both companies argue they have earned this right through a commitment to invest. But with the prospect of video entertainment being delivered internationally via broadband networks coming soon, are Hong Kong's interests best served by having little in the way of local competition to establish the best supplier of VoD or cable services?

5. Representing consumers.

What is the role of the Consumer Council in an era of convergence? The Consumer Council has long advocated the introduction of a general competition law and a competition authority. However, industry representatives have never been happy with the position adopted by the Council. One important reason for reinforcing the role of the Consumer Council and for focusing on consumer advocacy is to increase the number of people able and willing to go on-line. Chief Executive Tung Chee-hwa has identified technology as a key area for Hong Kong to develop if it is to remain ahead of competitors such as Singapore. The more the opportunity is disseminated through the community, the greater the opportunities will be.

Another motivation for pursuing consumer interests is that offered by public service broadcasters, who suggest that their role in offering cultural diversity and a plurality of views should be seen as a fundamental

counter-balance to private-sector forces answerable only to the bottom line.

Which brings us to the future role of RTHK . This has been set aside again and again. Now that the contours of policy towards convergence are set, how and when will the role of public service broadcasting be reassessed? How crucial to the issue of quality is it? Or will greater access to international broadcasters deliver the goods?

6. Regulating for an unknown future.

This returns to the issue raised at the end of the first section: for any location, will it be better to have good regulations or a good regulator? For Hong Kong, given its small size, its commitment to developing principally as a center for services, its open economy and its status primarily as a consumer not developer of digital products, the answer may well be the latter. What it needs is an information infrastructure responsive to the needs of users, which will change unpredictably over the foreseeable future.

But where will the regulator sit? Where will the regulator come from? And who will the regulator be? These are not simple, nor obvious questions. Hong Kong's telecommunications regulator, the Office of the Telecommunications Authority (OFTA), established in 1993, did an excellent job of achieving its objectives. Whatever one may think of those objectives, they were pursued consistently, and simply having the regulator there meant that a referee existed.

The same cannot be said of the broadcast sector. Currently Hong Kong has a policy-maker, the Broadcasting Authority, but no equivalent regulator. The need to establish independent referees to encourage convergence is perhaps one of the most important lessons to take from the experiences from elsewhere around the world.

Hong Kong is attempting to move beyond an era when regulation of broadcasting content was the primary consideration. The shift towards economic regulation is indicated by the lighter content rules governing the non-free-to-air broadcasters, but policy also indicates a desire to encourage content diversity which implies liberalizing the upstream content layer. Has the government gone far enough in specifying the forms of regulation required to bring this to reality? What changes in the role of the Broadcasting Authority (BA) and the Television and Entertainment Licensing Authority (TELA) are envisaged? Will these new roles require their reorganization, turning these bodies into more full-time organizations? How far will they deal with issues of concern to the industry upstream as well as downstream? Getting a clear perspective on these questions may turn out to be the critical factor for the success of the government's commitment to market liberalization, and the promotion and facilitation of content diversity and quality.

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