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Abstract

Although ten years have passed since Japan's telecommunication business was liberalized, development of the industry is so far only modest. Further deregulation is considered inevitable because it is widely believed that the business is stagnant chiefly because of the regulation. While debates are going on as to how and to what extent deregulation should be promoted, some discrepancy has emerged with respect to the framework of telecommunication regulation such as policy goal, policy instrument, and regulatory procedure.

In the standard theory of regulation, an efficiency criterion plays an essential role. As for Japan's regulatory administration, however, there is no evidence that this criterion has ever been ranked as number one. On the contrary, one can observe an inefficient policy-mix for promoting competition and natural monopoly-type regulation such as restriction of entry and tariff control. Another possible source of inefficiency can be found in the lack of transparency in the regulatory procedure, and in the tardy development of open network. Arguments against the regulatory policy are concentrated on those issues listed above.

The purpose of this paper is to clarify what is essential for Japan's regulatory policy in order to improve efficiency in the telecommunication business. As a matter of fact, there have been a lot of advice and recommendations announced toward more efficient regulation in the government as well as by business groups and scholars, of which only a few has been so far adopted. Being disgusted at the fruitless efforts, some argue for total abolition of economic regulation. The central question here, however, is not concerning whether the regulation be reformed, relaxed or abolished, but why efficiency is respected not so fully as other policy criteria.

While policy objectives are generally mandated to promote public welfare, general consumers are not endowed with the countermeasures reliable enough to ensure it for themselves. Thus the public access being substantially limited, and the regulatory process is vulnerable to the influence from interest groups. This means that the regulatory governance does not exist on the consumers' side.

Japan's regulatory regime as such seems now losing its economic rationale because the cost associated with the regulation is rapidly increasing due to expanding price gap of domestic-overseas market and because of the low economic growth.

1. Introduction

The purpose of the regulatory policy regarding telecommunication is to maintain

an environment in which the people who use them can obtain the utmost benefit from the telecommunications service. In today's informationalization of economy, there is an increasing need for telecommunication services. If those who provide services respond to such need under the comfortable regulatory environment, the telecommunication industry will no doubt make a remarkable development. Hence, a great expectation is placed on the telecommunication regulatory policy.

Telecommunication regulation is moving towards liberalization worldwide, which already has produced expected results. Japan, as well, promptly diverted its regulatory policy and liberalized the telecommunication industry ten years ago. The development of the industry since, however, was hardly smooth. In particular, in terms of preparation of networks for new services as well as the use of service, Japan is substantially behind the West and some of the Asian countries. Some attributing this situation to lack of the government initiative in policy, and others more to the cultural differences in communication, it would not be proper to give a clear cut explanation to it at this stage. However, a large majority agree that the regulation more or less has had a negative effect on the matter. A comprehensive review of the economic regulation is being made at the governmental level, in which deregulation of telecommunication has been hammered out. However, although there have been a number of deregulation attempts by the government in the past, none of them were thorough enough in their results and the expected effect has never been achieved. The discussion on deregulation has always been simply listing of technical issues where the vital points that existed at the start of the regulation tend to be missed. In view of the above, I would like to pay ample attention to the framework of the regulatory policy that should be coped with before proceeding to specific review of the regulation, although it may look like a round-about way of approach.

2. A View From Regulatory Framework

The core of the liberalization policy was to abolish the monopoly policy and encourage new entries so as to realize effective competition in the market. Introduction of competition was naturally welcomed by those firms who plan to make a new entry in the market. At the same time, new entries were expected to yield favorable market performance in the interest of consumers through competition, which, it was also expected, will be followed by a favorable cycling of further increase in demand and business chances.

The first step of the liberalization policy was to set up business sectors or divisions and to allow new entrants (Table 1) to enter the market segment under the Telecommunication Business Law and administrative guidance.¹⁾ Growth of the business is so far, in spite of the bullish expectation, depends upon the sectors. The largest sector, the subscriber telephone service, has grown at the lower rate, while the mobile service at the higher. The incumbent NTT's operating income has kept shrinking since 1987, and total sales has decreased in 1992 for the first time. The market growth is therefore said to be only modest as a whole (Table 2 and Table 3).²⁾ In the international service market, where the competitive environment is severest, the rate was reduced with the introduction of competition to the great benefit of the users (Figure 1). Moreover, this tendency has taken on a new development in which

Table 1 Number of Common Carriers

	1990	1991	1992	1993
Type I total	62	68	70	80
NCC	60	66	68	77
Long Distance	3	3	3	3
Local	7	7	7	8
International	2	2	2	2
Satellite	2	2	3	3
Mobile	46	52	53	61
Type II total	841	943	1,036	1,179
Specialized	28	31	36	36
Ordinary	813	912	1,000	1,143

Table 2 Market Size of Telecommunications Service

	(billion yen)						
	1987	1988	1989	1990	1991	1992	1993
Total Telecom.	6,123	6,268	6,548	6,996	7,555	7,908	8,192
Domestic Type I	5,566	5,462	5,698	6,050	6,313	6,615	6,864
NTT	5,238	5,344	5,482	5,655	5,746	5,574	5,496
Int'l Type I	247	257	260	266	291	303	328
Total Type II*	510	550	590	680	950	990	1,000
CATV*	24	27	31	37	41	67	69

Source: InfoCom (1994,1995)

* Estimated by InfoCom

Table 3 Domestic Market of Type I Service

	(billion yen)					
	1988	1989	1990	1991	1992	1993
Telephone	4,599	4,744	4,884	4,940	4,969	4,932
growth rate	—	3.15%	2.95%	1.15%	0.59%	-0.74%
Private	358	399	438	464	530	566
Mobile	84	136	247	340	467	630

Source: InfoCom (1995)

Table 4 NTT vs NCC (Telephone Sales Base)

	(billion yen)					
	1988	1989	1990	1991	1992	1993
NTT	4,530	4,595	4,654	4,618	4,577	4,530
share (%)	98	97	95	93	92	92
DDI + JT + TWJ	70	148	230	322	392	402

Source: InfoCom (1995)

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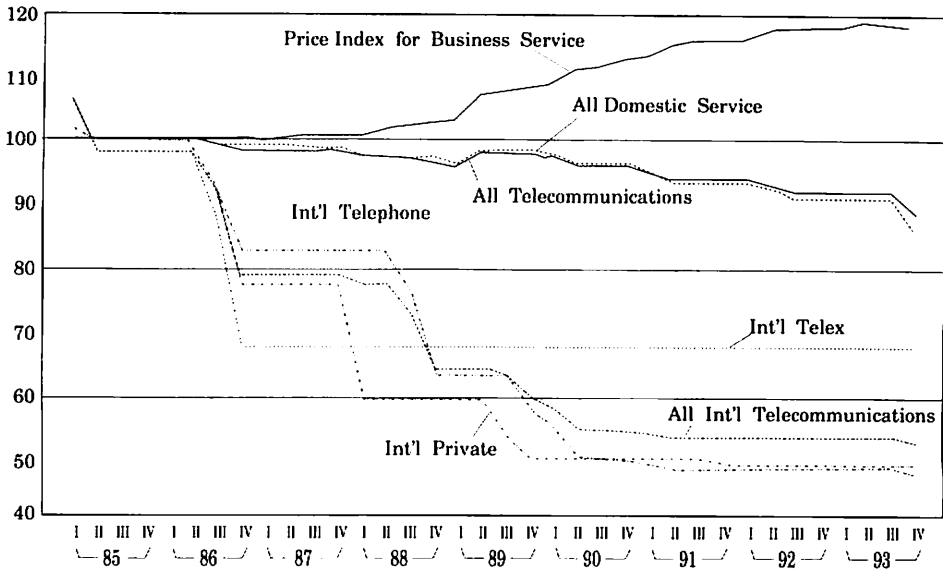


Figure 1 Transition of Rate Level of International Telecommunications Service

Source: Economic Planning Agency [1994a].
1985=100

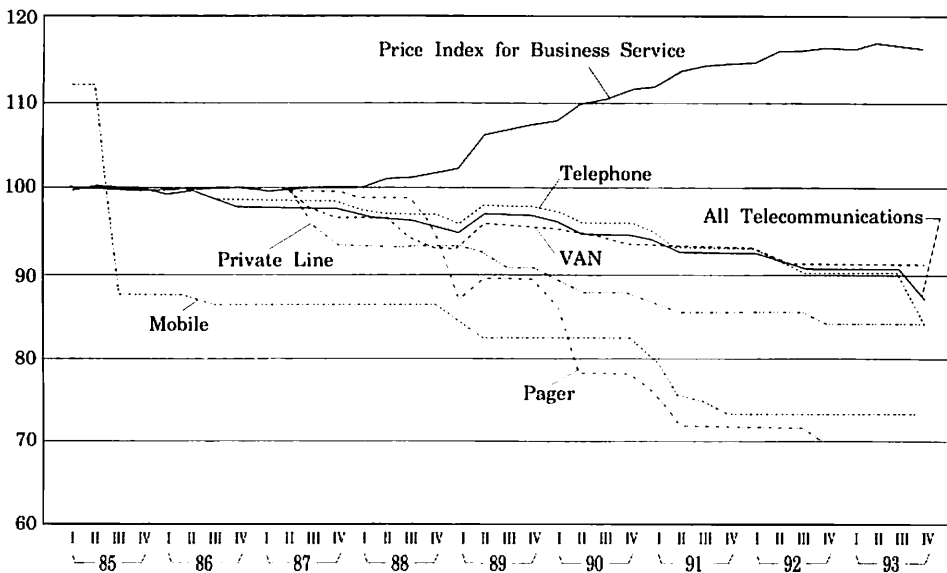


Figure 2 Transition of Rate Level of Domestic Telecommunications Service

Source: Economic Planning Agency [1994a].
1985=100

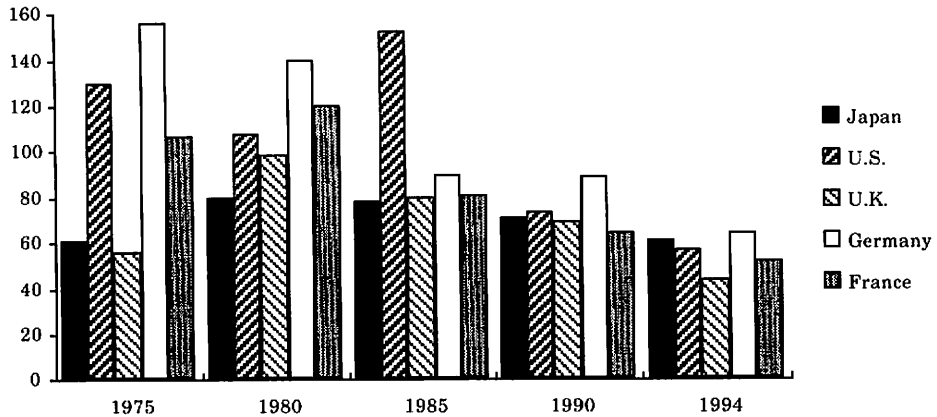


Figure 3 Comparison of Telephone Rate

Source: Economic Planning Agency [1994b]

1. Estimated on the basis of 1991 usage pattern in Japan
2. Yen rate is based on IMF's IFS
3. Thousand yen

users are shifting to overseas carriers because of the widening gap in the domestic-overseas prices due mainly due to the appreciation of yen. On the contrary, with the domestic service, in spite of the introduction of competition, NTT has still a large share in terms of total sales (Table 4), rate of services has been reduced pretty much but less than in the international service (Figure 2), users' choice out of rate menu is so constrained that they have no means to cope with the wide gap in the domestic-overseas prices (Figure 3).

With Type I business, although the market has been opened to the competition, a lot of regulatory elements under the monopolistic industrial organization still have been succeeded in the Law, and the regulatory policy was managed on this basis. This contradictory structure of the policy framework evokes a question whether this regulatory framework does serve promoting competition or create distortion. This question is closely linked with the various criticisms and reform suggestions regarding the criterion of demand-supply adjustment for facility licensing,³⁾ conditions for fair and effective competition, necessity and scheme of rate regulation, propriety of business segmentation, access charge and rate rebalancing etc.

Although the aim of this article is to search for the desirable direction of deregulation or reform of the telecommunication regulation, the subject will be treated from a little wider perspective, starting with such a fundamental question as what impact it may have on the economy, what is the rationale and objective of regulation, and who governs regulation. This is because it is very likely that the Japan's telecommunication regulation leaves those questions still suspending. In the following the discussion will proceed with focus on the three points, i.e. the domestic-overseas price differentials, the objectives, measures and cost of regulation and governance of regulation, and finally the individual issues will be briefly touched upon.

3. Regulation and Domestic-Overseas Price Differentials

In Japan the price differentials between the domestic and overseas market have become wider and wider of late. This phenomenon is found not only in the telecommunication industry but also in the service industry in general where no import-substitution is possible. In this context, the solution of the domestic-overseas price differentials should well be assigned mainly to the macro-economy. If, however, appreciation of yen proceeds, reflecting the changes in the real economy, some measures should be taken in the micro-economy field as well. Cost items such as labor cost and commission, whose price differentials between domestic and overseas market are larger, work as a stronger cost-push factor as appreciation of yen proceeds, hence total costs increase if there is no improvement in productivity. Needless to say, telecommunication service has extensive impact in terms of input-output relations. Under the circumstances where dependence on telecommunication service has been increasing due to the advance of informationalization, expanding gap between the domestic-overseas telecommunication service rate works as cost-push factor on tradable goods, and consequently affects the international competitiveness. In case where domestic market mechanism works well so that each firm has incentive to save the factor of higher cost on dollar base by substituting the lower cost one, the price gap between domestic and overseas will be under control. In view of this, the principle of competition should be effectively utilized so that it may provide such incentives. In addition to the direct cost of implementing the regulation, it can be itself a cause for incurring agency cost (which will be touched on later). These regulatory cost factors tend to increase as yen is appreciated because in general they are less avoidable. Further, regulations outside the telecommunication sphere such as regulation governing the right of way for circuit installation can be also a cost-push factor. Attention should be paid to the fact that these cost factors accelerate widening of the domestic-overseas price differentials, and therefore, even if regulation has any benefits, it will eventually work in the direction of canceling them off.

4. Objectives and Cost of Regulation

Many argue that regulation is often functioning as an obstacle against competition, thereby it is welcomed as industrial protection by incumbent firms. Although the argument is often the case for Japan's industry, too much emphasis on this aspect may jeopardize the basics of regulation. Particular attention will be drawn to the objectives and cost of regulation. Fortunately the literature of economic analysis on the public utility regulation provides us with a lot of findings which will help in dealing with telecommunication regulation. First of all, why is regulation necessary? Has regulation actually been effective? Is it fully recognized that regulation incurs various costs? What is the good way to achieve the goal of regulation while holding down the cost it incurs? A lot of discussions have been made about them and the outcome reflected in the regulatory policy. As a result

deregulation has been prompted where market competition is substitutable for regulatory measures, and today competition is being introduced also to the telecommunication fields worldwide. Where regulation cannot be replaced by competition, reform measures such as incentive regulation and franchise bidding have begun to be adapted. It can be said that Japan was forward in this respect as it already decided to, and actually introduced, competition ten years ago. As stated above, it is true that telecommunication services are now offered in a competitive environment. However, the result is not satisfactory and there are many questions as to the content of policy. This point is now further examined from the angle of the regulation theory. For this purpose, OECD (1992) is very helpful, in which there is an analysis on the background of regulation and reasons for its reform.

The entry and rate regulation of telecommunication industry has its economic basis in its natural monopoly. Technology under natural monopoly is such that the total cost is lesser if a certain quantity of goods is produced together rather than produced separately by two or more firms. With such technology, sooner or later, one single company will drive out its rivals and establish a monopolistic position. As a result, the consumer cannot expect to take advantage of natural monopoly (market failure). In this case, from the standpoint of securing efficiency of resource allocation, it was considered desirable for the government either to intervene in the market to run the telecommunication industry by itself, or countervail the strategic behavior of the monopolistic firm through entry and rate regulation. Therefore, if a technology has no natural monopoly, then there is no rationale for regulating firms.

Natural monopoly regulation was assigned with a goal to correct the inefficiency it accompanies. It was revealed, however, that regulation could provoke poor performance in a number of ways which is often referred as "regulatory failure".⁴⁾ That is characterized, specifically, by the stagnant productivity due to lack of competitive pressure, the quality standard which is set unnecessarily too high, and the protectionist advocate justified by the rationale of regulation in the particular industries. From the theoretical framework of the principal-agency model, this sort of regulatory failure is attributable to the fact that the behavioral objectives of the authority and firm do not actually coincide, but it is difficult to fill in the gap as there is asymmetry of information between them. Such cost which accompanies regulation is called agency cost. Agency cost is attributed to the regulator's dependence on the regulatee for information necessary for regulation, and as such, is reducible by taking measures accommodating incentives so that the regulatee himself behaves honestly. One example is the incentive rate regulation, which is designed so as to motivate the regulatee towards the optimal pricing. Franchise bidding is another, in which a license is granted through bidding in order to promote efficiency.

The above is an overview of what has been discussed about public utility regulation from the economics' standpoint and is established as a general theoretical framework. These theories are general enough to apply to any specific case as long as the assumptions of the model coincide with the actual conditions. When Japan's telecommunication regulation is reviewed on the basis of the above theoretical framework, it will be observed that it is not compatible in following points.

(1) Objectives and Rationale of Regulation

Regulatory measures are essentially assigned to the improvement of economic efficiency (efficiency of resource allocation). Actually, however, this criterion is rarely respected in the implementation of the Telecommunication Business Law or administrative guidance. This tendency is found, specifically, in the fact that efficiency has been taken less into consideration with respect to the implementation of the entry and tariff regulation, whose origin is obviously based on the supposed natural monopoly, as well as the liberalization policy whose central issue is how to arrange the playground conditions to promote fair competition (refer to the next item and item after next). It is also observed that when authorization is granted for new services, emphasis is placed on equal division of the business territory rather than equal chance for competition which may end up with improvement in efficiency, which is supposed to be a regulatory policy criterion, and the scope of business tends to be segmented into smaller divisions at the cost of economy of scale and economy of scope.⁵⁾

(2) Propriety of Natural Monopoly Regulation

The combination of entry regulation and rate regulation is a typical method of natural monopoly regulation. It is theoretically a contradiction to put regulatee firms under a competitive environment while employing those regulations. Namely, it will cause inefficiency if entry of two or more firms is admitted in a technological environment where natural monopoly is dominant. On the contrary, it may cause inefficiency if the similar regulation is implemented in an environment of non-natural monopoly technology.

(3) Preparation of Conditions for Fair Competition

In order to promote liberalization policy it was necessary to create an environment in which new entrants (NCC) could compete with the incumbent (NTT) under fair competitive conditions. On the other hand, it was also expected of NTT that it would show better achievement as a privatized enterprise. It was, therefore, the tenet of the liberalization policy to attain both of those goals while maintaining an adequate balance between the two. As is clear from the above, the policy should have been designed and implemented within the theoretical framework based on the different principle from the natural monopoly regulation. In Japan, however, the framework could be hardly identified because measures such as the so-called infant industry protection were applied to achieve the above goals in combination with those designed for natural monopoly regulation.⁶⁾ A good example of the efforts made by the government for creating a market environment which enable effective competition between the new entrants and the strong incumbent is found in the anti-trust policy or the dominant regulation in the US. in the 70's and 80's. However, the methods applied are obviously different from those of Japan. By the way, one of the necessary conditions in order to create and sustain such a market environment is that, the market is not to become zero sum, in other words, the market is expanding at a sufficient rate so that it enables every player to enjoy sustainable growth. The

circumstances of the telecommunication market in Japan was less favorable for the policy than in the US.

(4) Transparency of Regulatory Administration

It is pointed out about the telecommunication administration, as is commonly seen throughout the administration as a whole, that there is a tendency that important regulatory policy, such as setting up business segments as a licensing guideline, introducing the so-called asymmetric regulation and so on, often takes the form of an administrative guidance so that the contents of policy and procedure of decision making are not transparent enough.

I would now like to examine in more detail the relationship between the two concept of the lack of transparency of administration and the asymmetry of information mentioned above. One can consider that the regulatory system consists of two phases, i.e. citizens⁷⁾—regulator relationship and regulator—carrier relationship. In theory each concept would make sense in the context of each relationships. But their actual meaning is different between the two relationships. With the former relationship, intransparentness (defined as lack of or shortage of transparency) of administration means that the citizens don't have easy access to the information of administration, and what is meant by intransparentness in this context is almost the same as what is meant by the asymmetry of information in the framework of the principal-agent relationship, that is; principal-citizens and agent-regulator. In this context of the relationship, possible failure associated with intransparentness of administration is closely related to the regulatory governance, which is explained extensively in the following paragraph. On the other hand, with the latter relationship, intransparentness exists in actuality on the administration's side, not on the carriers' one who are regulated, so that they do not have a clear sight over the administration, while asymmetry of information means that the regulator doesn't have easy access to the carriers' information, and therefore, the two are contradictory in this point.

Intransparentness is a problem because it makes the regulatee bear unfair cost of regulation. Then, does the asymmetry of information also matter for this relationship? As will be discussed later, the author thinks that the regulator-carrier relationship in Japan is more close to that of a "guarantor" (Samuels [1987])⁸⁾ than that of a principal-agent relationship. Therefore, it is the citizens-regulator relationship, not the regulator-carrier relationship that it is proper to analyze its agency cost of the regulation on the basis of the principal-agency model. With Japan's current administration-business relationship given, one of the conclusion which could be drawn from this proposition is that, any attempt for an incentive regulation designed to overcome the asymmetry between the regulator and carriers will not make any sense, and which is ironically endorsed by the fact that it has so far encountered consistent resistance in Japan.⁹⁾

(5) Open Network

In order to realize fair as well as effective competition, a policy direction has been shown that, interconnection with, and use of, the NTT network would be opened.¹⁰⁾

With regard to provision of network service to type II common carriers, public-private-public interconnection and ONP(open network architecture) are awaiting realization. Recently, however, interconnection with NCC for provision of new service is has been highlighted. With regard to interconnection between type I common carriers, the concept should naturally differ depending upon whether the network connected is monopolistic or competitive, infrastructure or not.

To provide a theoretical framework, let us consider two extremes, one is the case of infrastructure, provided monopolistically with network externality, the other extreme will be that of interconnection between carrier in an competitive environment with negligible externality. In the former case, it is desirable that the network's external economy and benefit as public goods are shared widely by users in general. Therefore, it is reasonable that access charge is determined on cost base and by parties who use the infrastructure. The lower limit of total access cost is the incremental (marginal) cost required for a new access, which is shared by users. Regulation may be effective in order to obtain desirable results.

In the latter case, in contrast with the former, it is desirable to be left to bargaining among the parties concerned on an equal footing so that access charges and other conditions necessary for the interconnection can be determined in an efficient manner through market mechanism. In general, interconnection of networks entails transaction cost, especially initial cost may be much larger than that of ordinary service due to the tedious technical adjustment. Well-established technical standards for network and equipment as well as well-designed property right for network interconnection and operation will reduce transaction cost.

As far as the interconnection of network is concerned, most cases will fall between both extremes. In Japan it remains vague which telecommunication service is provided in the competitive market. According to the Business Law, the Minister is endowed with the authority to allow introduction of competition in all areas of services including the basic service provided by local networks. It is therefore difficult to distinguish which network or service can be seen and to what extent it is treated as an infrastructure. A principal criterion for determining that a certain network can be attributed to infrastructure is that it has substantially no substitute and that it is widely used.

According to the criterion, NTT's local network service for the end users except for the larger business customers comes under infrastructure. If this is true, however, it will lead to some contradictions. First, while NTT is responsible for the operation of the infrastructure on the one hand, it is run as a private enterprise and is faced with other common carriers as rivals. Further, while it is desirable that the total access cost (i.d. the cost of the infrastructue) be shared among all the long distance carriers including NTT's long distance sector, NTT, being a private enterprise, does not have an incentive to share the costs incurred for the convenience of other firm(s). These contradictions may be resolved by structural separation of the infrastructure portion of the network, which, however has been considered hardly possible in reality. A second best would be to establish a rule for an open access to the infrastructure portion and cost-sharing by the firms concerned including the NTT's long distance sector.

5. Regulatory Governance and Its Cost

In the preceding paragraphs Japan's regulatory policy was examined with reference to the theoretical framework of the public utility regulation. As I briefly mentioned there, the problem of regulatory governance seems to make an important theme to be scrutinized because of its relevance to intransparent regulatory administration. Regulatory governance, if it is appropriate to call it so, concerns the framework of authority and responsibility with which the regulatory agency who are assigned with public utilities administration by citizens should conform when making decisions and enforcing them.

Chiefly from the viewpoint of the US., Spulber (1989) describes that regulation involves both direct and indirect interaction between the regulatory agency and players in the markets.¹¹⁾ In this aspect, the regulatory process in the US. and Japan looks pretty much the same. However, there is a lot of difference in the manner as to how and to what extent the regulatory agency actions are governed, which are central in rule making and enforcement in both the countries. The Federal Administrative Procedure Act requires, for instance, that the agency must allow interested individuals "an opportunity to participate in the rule making through submission of written data, views, or arguments with or without opportunity for oral presentation". In contrast to the US., in Japan, important decision making including rule making, authorization of license, issue of order etc. always takes place in a closed club such as advisory committee, to which, while deliberately selected persons from interested business groups, user groups, and consumer groups have only an access, a public access is substantially restricted.

The citizens-regulator relationship being thus characterized in Japan, the first point of the issue concerns divergence of the policy goals between them. As mentioned in the preceding paragraphs, with respect to the policy goals, an emphasis had been put on the nurture and the protection of industries, rather than the improvement of efficiency. In this sense there is little evidence that in the regulatory policy decision the priority is given to the general interest of the citizens, above all, that of the consumers.

The second point of the issue is that, is there a system to reflect the consumers' opinion on regulatory administration as much as possible? From the user's view, freedom of information is insufficient, there is not enough transparency in the decision making process, and the administrative procedure is so poorly designed that they are not given enough opportunities for expressing their opinion. Under such circumstances general consumers are hardly to check regulatory policy. In view of independence principle of the regulatory administration from the direct intervention of political power, what general consumers can do to protect themselves would be limited at best to the use of common suffrage or sending in a voice to the carriers concerned. In other words, they have substantially nothing to reflect their opinion on. It could be said that regulatory governance is practically out of reach to the general public.

The third point is that the cost incurred from the fact that regulatory governance by the consumers is imperfect could be high. With a system where administration is practically free from consumers' check, the weaker the check is, the closer to the regulator itself the regulatory governance resides. Under such circumstances the

regulator tends to be more easily influenced by interest groups. As suggested in point 1 above, if the goal of regulation is not in the interest of the general public, but rather in the special interest of a particular group whose interest conflicts with that of the former, the possibility is high, that the consumers should be satisfied with a relatively low welfare level compared to what they could have enjoyed otherwise. And the difference is nothing but cost of regulation.

It is widely observed in the regulatory process that the carriers' interest tends to be weighed over the users' when authorization, a typical instrument of regulation, takes place. Normally, an authorization system itself has legal ground, for the Diet has approved it because of its rationale, the promotion of the general interest. Once introduced, however, the incumbent will take advantage of the authorization system as being a barrier to entry (refer to Stigler [1975] for analysis of the similar cases in the US.). Firms are involved in rent seeking activities in pursuit of such benefit, and approach the regulator, so that the regulation is implemented in their interest. If an authorization system becomes a barrier to entry, the incumbent enterprises will be able to escape competitive pressure so that the efficiency level of management will be lowered. Consequently, the consumer's choice will be more constrained.

Let us now go back to the topic of telecommunications regulation and carry on our discussion taking the case of asymmetrical regulation. The point is, whether or not it served the general interest. Competition was introduced by the liberalization policy but whether it would end up with "effective" one or not depended on whether NCC, the new entrants could smoothly expand their business. Especially in the long distance telephone service market, the key was whether they could successfully confront the incumbent NTT. It seems that the government had two major policy options then. One was to place regulatory handicap on NTT and the other was to treat NCC favorably. The actual government policy was inclined to the latter. NTT's rate of the long distance service sector at the time of liberalization was set at a high level way above the cost, hence large amount of surplus has been generated, which supplements the deficit of subscriber line and directory assistance (Table 5). So there was enough room for profit for NCC if it provided service at a rate a little lower than NTT and that helped NCC's business growth (Table 6).¹²⁾ On the other hand, it can't be denied that, because of this, NCC tended to rely on regulation and NTT's rate rebalance lagged as well as the management efficiency efforts were slowed down. There also a big loss in consumer's surplus due to that distance service rate exceeded average cost for a long time. It remains a question which option was better for consumers in general.

Table 5 NTT's Operating Profit/Loss in Detail

	(million yen)				
	1989	1990	1991	1992	1993
Subscriber Telephone	865,123	742,963	668,404	561,960	372,317
Subscriber Line	-161,472	-189,935	-155,364	-148,520	-164,811
Local	-13,892	-3,216	20,330	24,781	31,416
Long Distance	1,048,897	954,368	812,933	689,571	521,107
Directory Assistance	—	-226,716	-184,332	-173,444	-160,634

Source: NTT

Table 6 Operating Profit of NCC

	(million yen)			
	1990	1991	1992	1993
DDI	25,619	31,809	32,223	30,047
Japan Telecom	20,520	27,936	32,073	25,664
Teleway Japan	1,581	-3,534	-4,346	-8,074

Source: InfoCom (1995)

6. Will Regulatory Governance Change?

In the preceding paragraph, we discussed that regulatory governance resides on the administration's side. We also know from the above that in spite of the government's claim that the policy goal is promotion of the general consumers' welfare, they have neither a secured access to the regulatory procedures nor freedom of information enough to protect themselves against unfavorable treatment. As for the administrative organization in Japan, the regulatory authority is integrated to the respective ministry, is held practically by bureaucrat and significantly independent from legislative and judicial check. The government offices, especially ones dealing with economic matters, are closely related with economic world through the respective business organizations or groups they deal with. Moreover, politicians find themselves playing an intermediary role between the government and business. Thus politicians, business men and bureaucrat together have enjoyed "the iron triangle" coordination. Administrative process is, therefore, not independent from political and business influence. As a result, in actuality presence of policy bias towards the business interest groups is possible.

It was not before the policy shifted into the liberalization of telecommunication business that the telecommunication administration took its current structure. Nevertheless, MPT (Ministry of Post and Telecommunications) was not an exception to the traditional Japanese administration system and the business world also seems to have been receptive to such system.

It is said that many of the characteristics of the modern administration system of Japan has been formed in the framework of the so-called "the Showa 16 (1941) regime", the national mobilization regime in the wartime period. It was a convenient system for effectively executing plans towards a totalitarian goal like execution of the war. Although the goals are different, the system was carried over to the postwar period and its characteristics are found in the measures like administrative guidance. Under the political stability called the long-lasting "1955 regime", during which LDP hold political power, the government offices dealing with economic matters employed the policy to nurture industries, were accepted as "guarantor", as Samuels (1987) describes, who lead manufacturers to success, and deepened their interdependence on business world. The system was effective in protecting the interest of the industries concerned, but did not necessarily link itself to the improvement of economic welfare of the consumers. Because regulatory governance is on the administration side, regulation is no longer used as a specific policy measures for the improvement of welfare but has become an all-round instrument for

administrative management and control. For the same reason, as Johnson (1982) argued referring to "development oriented state", the role of administration is no longer that of a referee of the rules of the game where the private entities are principal actors, but that of a leader who seeks to realize a specific ideological goal set by the state. Even in case where competition was encouraged as a policy, besides the efficiency objective, which is usually expected of competition, there is probably another aim of making business chances open for the sake of the industry world. thereby the latter should not be underweighed.

The system worked, if not well, in the days of high growth where success of enterprises made possible a continuous increase in wage level and benefit of growth was extended even to small investors. But as we enter into an era of a strong yen and low growth, the system has began to show its more evil than good. Regulation sometimes resulted in protection of low productivity industry or outdated system, thereby hampering the emergence of new service to narrow consumer options. Further, the cost of regulation either directly or indirectly falls on firms and consequently is reflected in the price of the product. Thus, the disadvantages can no more be ignored. As the growth of wage rate is leveling off, the consumer begins to have dissatisfaction in the administration with priority to industry. When the economic structure is changing with certainty like this, if bureaucrats try to maintain their traditional behavioral pattern and if they have a structure to allow it, it is natural that discussion now goes beyond policy level and criticism to bureaucracy governance itself increases. Sakaiya (1994) is an example of such criticism who claims, "Today, there is a cry for deregulation and reduction of fiscal expenditure. The biggest obstacle therefor is bureaucrat's morale decadence, in other words, the psychology that takes protection of group interest as social justice". Here the criticism concerns not only bureaucracy but also a state view itself.

7. Conclusion

Throughout this paper, focus is put on the efficiency criterion in the regulatory policy making of Japan. Policy switch in telecommunication from regulation to competition is now worldwide megatrend, thereby efficiency gain in the industry is expected. I have begun with the subject by raising the question, however, why telecommunication business in Japan remains so modest, despite the fact that the competition was introduced in the market as early as 10 years ago. Regulation can be actually attributed to the inefficient performance of the business. Scrutinizing the way in which regulatory policy is made and enforced, it becomes evident that it was not to the policy goal of improving efficiency that the top priority has been given. A consequent question is who governs the regulatory process. It is argued that the regulatory governance is held mostly by the regulatory agency, which may be another source of inefficiency.

What is really needed for Japan's telecommunication deregulation? This first and the final question inevitably entails with equity judgment besides efficiency question, which is beyond the scope of this paper. The key to the question accordingly depends upon what solution is to be given to the following problems, which will be proceeding step by step on the basis of the discussion above.

— Total deregulation or wise regulation?

Should regulation be totally abolished and substituted with competition? Or should regulation be modified and relaxed along with further and simultaneous reform of administrative procedure?

— For whom regulation is made?

Should an efficiency criterion be respected at least as well as the other criterion, if the goal of regulation is to promote public welfare? What is then necessary to assure efficient solution in terms of consumers' right vis-a-vis regulatory authority?

— Competition, regulation or their combination?

Is any combination of competition and regulation suspicious from the viewpoint of efficiency goal? What is then the substitute for the inefficient combination in order to get to the goal of the fair and effective competition?

—Is the demand-supply adjustment criterion necessary?

Does this criterion happen to be the center of basis upon which any combination of competition and regulation is justified, for instance, with respect to right of way for public utilities?

—What would be the concept of the open access? Who bears its cost?

Would it be an obstacle against the open access to the local network if the incumbent who controls it claims the "fair share" of the interconnection cost?

Notes

- 1) Besides incumbent carriers (NTT, KDD), Type I business is segmented into the following categories: long distance, local, international, satellite, mobile. mobile business is further segmented into: mobile telephone, pager, personal handy system (PHS), CRP, marine service etc. As of April 1 of 1993, the number of Type I NCC amounts to 77. See Table 1.
- 2) So far the total turnover of the whole telecommunication services has been growing at about 5% (See Table 3), which is said to be modest. However, taking potentiality of Japan's information society into consideration, this figure is less than expected, especially for CATV.
- 3) Demand-supply adjustment criterion is mandated in the Telecommunications Business Law as the necessary condition for the approval of the authorization of Type I business license.
- 4) As for the source of regulatory failure, OECD (1992)'s surveys various factors such as divergence of objectives which the regulatory authority and the enterprise really pursue, managerial restraint by the regulatory oversight etc. See p.17-.
- 5) Once a license is given, Type I carrier should build all the facilities and circuits necessary for the business in principle even if there is potential scale economies through joint use of the facilities among the carriers. A typical case is TWJ, one of the long distance NCCs. It gave up the initial strategy which had targeted the "megalopolis", started building networks all over Japan, which would be unnecessary for TWJ, if it could have managed to provide the other area than megalopolis by leasing circuit or consigning business.

Another case is PHS. It was permitted as a Type I business in 1994 with the

license given to operating base station, not the whole system. PHS is one of the local network services which is expected to be substituted for the fixed local loop system due to cheaper usage. Authorized rates are, however, disappointing. They are pretty much higher than ones of the existing telephone service, reflecting high costs caused by the duplication of facilities and circuits.

- 6) Let us take a brief look at the remarkable take-off of the new long-distance service carriers. The two of three NCC companies, DDI and JT have been "raised" in a few years to be the national carrier. The three entered the market in 1986, then already in 1989 all of them have recorded the ordinary income above break-even. As for the fiscal position of the three in 1989, the aggregated ordinary income-total capital ratio was 13.1%, whereas NTT's was 4.6% (White Paper on the Posts and Telecommunications 1991). NCC's share in the telephone service, which was 1.5% in 1989 in terms of total revenue base, amounted to 8.1% in 1993. As far as the traffic between Tokyo, Osaka and Aichi is concerned, the NCC's share has grown tremendously from 39% in 1989 to 54.4% in 1993.
- 7) "citizen" is used as a general term which stands for all the private entities including larger and smaller business users, end users, consumers, type I and type II carriers, vendors, and even foreign interest groups.
- 8) This concept is explained in the section 6.
- 9) An example is the fact that MPT opposes introduction of the price-cap regulation.
- 10) For example, MPT Open Network Council (1992) and MPT (1994).
- 11) According to Spulber (1989), p.70-, "direct interaction occurs through public hearings and the rule-making process... Indirect interaction refers to the attempts by consumer and firm interest groups to influence regulatory decisions through legislative, administrative, and judicial channels.
- 12) See also the above note about NCC.

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