

# Privatization in Telecommunications



\*Deputy General Manager NTT Bangkok Representative Office Nippon Telegraph and Telephone Corporation

---

## ***1. Introduction***

---

On April 1, 1985, Nippon Telegraph and Telephone Public Corporation (NTTPC) was privatized to become Nippon Telegraph and Telephone Corporation (NTT). It's expected that NTT will be operated more flexibly under the condition of more or less equal footing with other competing enterprises.

---

## ***2. Reform of the Japanese Telecommunications System - Introduction of Competition, and Privatization of NTT***

---

### **2.1 Background of the Reforms**

NTTPC was a public enterprise established in accordance with the Nippon Telegraph and Telephone Public Corporation Law, and its activities were limited to those approved by Law. For instance, it was necessary to make up a budget for each fiscal year and then submit it to the Diet for approval together with associated plans of execution measures including funding. Flexible management of the corporation was difficult for many reasons, such as this budgetary control virtually identical to that imposed on the administrative agencies even though a self-supporting financial system had ostensibly been adopted. In the area of labor-management relations as well, the employees of the corporation were regarded as public servants and thus strikes were banned in compliance with the Public Enterprises Labor Relations Law.

And the environment in which telecommunication activities were being carried out had also undergone a drastic change, seven important examples are as follows.

(1) Customer's needs were rapidly becoming more sophisticated and diversified.

(2) An uneconomical aspect of double investment was being weakened due to the emergence of various new media (e.g., optical fibers and communications) resulting from technological advance.

(3) The necessity for across-the-board technical standardization was decreasing due to advance in interface technology, improved telecommunications equipment performance, etc.

(4) Demands were increasing for more rapid and active realization of more efficient telecommunications systems which could be able to serve as the infrastructure for enhancements of Japan's industry and economy.

(5) Private enterprises were becoming more willing to participate in telecommunication activities using their accumulated capital and technologies.

(6) Movements were under way in the U.S.A. and U.K. to increase competition in the telecommunications field.

(7) Proposals were made by the Second Ad Hoc Commission on Administrative Reform, as well as the Federation of Economic Organizations (Keidanren), etc. to the effect that the management form of NTTPC should be thoroughly reviewed.

In view of these environmental changes in the telecommunications field, it soon became of vital importance to realize more active and efficient telecommunication activities through introducing the vitality of a private enterprise and to turn the Telegraph and Telephone Corporation into a private company so that it could be operated more flexibly, on an equal footing with other competing enterprises.

## 2.2 Aims of the Reform

Several effects can be expected in the future from the major system reform.

(1) Demand will increase for a wider range of telecommunications services, the telecommunications market will be greatly expanded and activated.

(2) Introduction of competition is expected to cause overall service costs to go down in the long run.

(3) Introduction of the vitality of private enterprise into the telecommunications service business field will cause the telecommunications service industry to become both more efficient and more active. This in turn, will accelerate technological innovations, thereby contributing to the development of Japan's economy and society.

(4) Under the new system, Nippon Telegraph and Telephone Corporation (NTT) is allowed virtually complete independence, this will permit more flexible and efficient business operations, and allow NTT to establish a firm financial foundation.

---

## 3. Telecommunications Business Law

---

### 3.1 Character of the Laws

Industries are generally recognized under various enterprise laws as falling into three categories. First is a monopolistic form in which a single corporation is granted a monopoly. Second is a form where more than one enterprise is engaged in business under the control of an enterprise law. Third is a form where business is carried out in free markets under minimum legal control.

Activities as a telecommunications service enterprise have been carried out by NTTPC and KDD on a monopolistic basis under the Public Telecommunications Law

## 3.2 What is a Telecommunications Enterprise ?

The Telecommunications Business Law stipulates that a *telecommunications service enterprise* is an enterprise which offers telecommunication services to others who need them. Not covered are wire radio broadcasting, wire broadcast telephone and wire television broadcasting, which are controlled by their respective laws.

*Telecommunications services* are defined as "conveying the communications of others through use of telecommunications equipment, as well as offering telecommunications equipment for others' communication purposes". Included among *telecommunications equipment* are "machinery, devices, lines or other electrical equipment employed to perform *telecommunications* (i.e. transmitting or receiving codes, sounds or images by wire, radio or other electromagnetic means)".

The law also stipulates that a telecommunications enterpriser is an organization granted permission to, or registered to, or from which notification has been received concerning the intention to conduct telecommunications *business* activities.

### 3.3 Classification of Telecommunications Enterprises

#### 3.3.1 Type I telecommunications enterprise

Type I telecommunications enterprise is defined as "The enterprise that offers telecommunications services through the installation of telecommunications line facilities (transmission line facilities connecting sending and receiving locations plus switching facilities installed as part thereof, and their support facilities)". This type of enterprise accordingly needs to be highly stable, for the following reasons.

(1) Large capital outlays are normally required. Large numbers of people are also significantly affected by these enterprises actions.

(2) This type of enterprise provides the basis for all (Type II, etc.) telecommunications service offerers.

(3) Line facilities occupy space, land near roads and radio waves which are common social property and which may not be used freely just as anyone wills.

(4) The line facilities are often "rooted" deeply in each specific region, and thus may not seem to be readily replaceable by users.

Under the present Telecommunications Business Law, if a specific service, (say data communications service or telephone service) is offered by a Type I telecommunications enterprise, regulations intended for Type I telecommunications enterprise are applied in respect to charges, etc. If, on the other hand, the same service is offered by a Type II telecommunications enterprise, there will be almost no regulations imposed on his activities.

### **3.3.2 Type II telecommunications enterprises**

A Type II telecommunications enterprise is one not belonging to the Type I telecommunications enterprise category.

Based on the character of an enterprise and the scale of facilities it employs, Type II telecommunications enterprises are further classified into the following sub-categories.

(1) Special Type II telecommunications enterprises: Enterprises which satisfy the demand of an unspecified number of people, and which employs 500 or more lines to terminals operating at rates of 1,200 b/s x 5 lines for lines of 9,600 b/s or over). Enterprises offering international telecommunications.

(2) General Type II telecommunications

enterprises: Enterprises not falling under the above category.

Special Type II telecommunication enterprises are expected to have a significant effect on the people, thus it was felt necessary to regulate them separately from other enterprises. It should be noted that this special/general distinction was not based on the type of service offered, similar to the case for distinction between Type I and Type II telecommunications enterprises. There was a heated debate about how to regulate Type II telecommunications enterprises (including this special/general distinction) both during deliberation at the Diet and during Japan-US negotiations.

---

## ***4. Nippon Telegraph and Telephone Corporation Law***

---

### **4.1 Necessity of Special Company Laws**

The two main reasons a special company law exists for NTT are:

(1) Certain continuing influences NTT has brought on.

(2) The necessity for the government to hold part of its stocks.

### **4.2 NTT Management Aims and Conditions**

NTT was reorganized, on April 1, 1985, into a company with a capital of 780 billion yen and 318,000 employees. Management conditions need to be considered if plans are to be laid regarding future business development. Primary NTT management aims and conditions may be outlined as follows.

(1) NTT is a company oriented towards carrying on domestic telecommunications service activities. In addition to domestic telecommunications business, it can also

conduct related business activities as well as business activities, as approved by the Minister of Posts and Telecommunications, which must be carried on in order to attain the objectives of the company.

(2) NTT is responsible for (a) maintaining proper and efficient management, (b) helping to ensure that telephone services are offered on a stable basis throughout Japan, and (c) contributing to improvement promotion of R&D into telecommunications technologies (both basic research and applied development) and through the spread of the results of such research. The ultimate goal of these attempts by NTT is to promote the welfare of the people

(3) In regard to NTT stock, the following is the case

(a) The government is to at all times hold at least one-third of NTT's issued stocks.

(b) The Diet shall decide on the number of stocks to be disposed of during budget deliberations for that fiscal year.

(4) Being a semi-governmental agency, NTT formerly had to have its budget approved by the Diet. Hereafter, NTT will have its annual business plan approved by the Minister of Posts and Telecommunications. NTT is also controlled by the government through the need for approval by the Minister of Posts and Telecommunications in nominating or replacing directors and auditors, as well as in altering the corporation's articles of association and in disposing of profits. However, the stated objectives of the current reform was to promote independence in business management, thus official regulations by the government are limited to only those that are indispensable.

(5) Three major labor laws (the Labor

Standard Law, Labor Union Law and Labor Relations Adjustment Law) are applied in place of the former Public Enterprises Labor Relations Law. The right to strike is, in principle, approved. However, since NTT provides a public utility, certain limitations are imposed on strike action.

(6) Like ordinary companies, NTT is allowed to freely invest in business ventures.

---

## ***5. Reorganization of NTT***

---

A function-based organization would not be able to ensure that business would be carried out with a degree of the flexible mobility required in a dynamically-changing business environment, the conclusion was soon arrived at that a division system, common within private companies, should be adopted upon privatization.

### **5.1 Organization of Division to Prepare for Competition**

The first consideration in organizing divisions in this manner was thought to be separation of the department that offer trunk telecommunications network facilities (the Telecommunications Network Sector) from the customer service departments (other divisions). This conclusion was arrived at due to the following reasons:

First, telecommunications facilities (especially key line facilities for traffic between Message Areas (MAs)) would need to be integrated, and that they should preferably be operated on a unified basis. It was also expected that services would become more and more sophisticated and diversified, and would be affected by competition in each area. It was therefore thought desirable to create an organization that could react flexibly and responsively with a clarified structure drawing where responsibility would lie.

Provision of subscriber-associated facilities (Local Switches (LSs), Toll and Local Switches (TLSs), subscriber lines, etc. for traffic within MAs) is closely related to sales demand. Thus it was felt they should be held by telephone service divisions which would be oriented towards customer service.

Another consideration, then, was the division of customer service departments, an organization consisting of eight service divisions was worked out as a result of taking into account the special features of telecommunications services and customer needs while allowing for anticipated sales volumes, and future possibility of new or expanded undertakings.

Yet another consideration was the need to establish a system for the sale of customer equipment (communications terminal equipment). The network and customer equipment had previously been handled as a single entity at telephone offices; the users are likely to call for a higher level of services in the future; and that priority needed to be given to stimulation of more effective activity at the telephone office to ensure more efficient business management. Customer Equipment Division was set up to deal mainly with customer equipment development, purchase and wholesale distribution to each region. This service department has been called "Customer Equipment Service" to make the departments activities seem more familiar and easily understandable to customers.

## **5.2 Establishment of Strategic Functions and Streamlining Managerial Structures**

At the founding of the new company, an overall managerial strategy and technological strategy needed to be worked out.

Plans for business expansion (such as establishment of new business ventures and investment in subsidiary companies) had to be quickly and effectively laid. To achieve this, a Corporate Strategy Planning Headquarters and Engineering Strategy Planning Headquarters were established as separate entities from the service divisions.

Each service department (other than telephone service) was made into a separate division so as to be able to cope with demand trends and competition.

---

## **6. New Entrants into the Telecommunications Service Business**

---

### **6.1 Entrants Undertaking to Offer Type I Telecommunications Services**

Amendment of the telecommunications statutes enables entrance into all fields of the telecommunications industries by a variety of new entities. Actual and potential new entrants show interest in participating in the toll trunk line field. In this area, the profit making potential looks particularly good with use of the latest technologies (optical fibers, etc.). Constructing such new basis facilities as trunk line cables requires considerable land allocation and large-scale civil engineering. Therefore, the Japan National Railways, Japan Highway Public Corporation, and electric power utilities, which can use existing facilities such as channels along railways, expressways and power transmission lines can easily enter this field. Communications satellites will also be used because the costs of launching and operating communications satellite of a larger capacity are being reduced.

Projections by the Media are for new entrants to Type I category to begin business

in the trunk transmission area. Three new enterprises are presently progressing with plans to start up operations. One plans to use microwave lines, another plans to install optical fiber cables in channels along railway lines, and the other plans to install optical fiber cables along highways connecting Tokyo, Nagoya and Osaka. Three other groups are planning to incorporate and enter the satellite communications field.

## **6.2 Communications Line Liberalization and Trends Regarding Type II Telecommunications Service Suppliers**

In principle, there are no legal restrictions on Type II enterprises. When an enterprise is founded, this fact must simply be reported to the Minister of Posts and Telecommunications. However, special Type II suppliers, who will be providing many unspecified users with large-scale network services, must go through a registration process with the Ministry of Posts and Telecommunications in order to secure safety and reliability for users.

There are no restrictions as regards foreign capital. Foreign capital can be used arbitrarily in starting new business.

The new Telecommunications Business Law frees use of the lines, and so users can arbitrarily use the lines within the scope of their contracts. Many enterprises are accordingly planning to enter the VAN industry which had previously been restricted.

## **6.3 Reaction of NTT to Activities by New Entrants**

NTT is responsible for providing the whole country, including remote islands and rural areas, with reliable telephone service. It is anticipated that new entrants will become powerful competitors because they are able to start their business providing service

in the highly profitable area of communications between large cities, using the latest technology and the optimum number of personnel.

NTT therefore will need to improve its operating efficiency and rationalize its management in way that are not unfair to the new entrants. NTT will need to compete with the new entrants while at the same time it is cooperating with them. When NTT is requested to supply necessary information to these new entrants, it will thus cooperate on a case by case basis with in the guideline of competing principle.

---

## ***7. NTT's New Business Activities***

### **7.1 Thinking Underlying New Business Development**

#### **7.1.1 Basic concepts**

NTT plans to actively and flexibly promote new business operations, expansion of operational areas, and formation of a wide range of improved working environments to stimulate employees. This will be done through effectively taking advantage of the technical and managerial know-how and resources that has accumulated over its years of operations, as well as through studying and availing itself of the benefits to be gained from competitive market and privatized operations.

#### **7.1.2 Procedures for developing new businesses**

The New Business Development Office was established in the Corporate Strategy Planning Headquarters at the birth of the new NTT in April, 1985. The New Business Development Office has been planning overall entry into new business areas, planning strategy, searching for new business ideas, and undertaking feasibility studies regarding new business ideas, reviews of the possibility of joint ventures with other enterprises, areas

for capital investment, and transfer of NTT personnel to new business enterprises.

### **7.1.3 Transfer of Personnel to Subsidiaries**

NTT will be transferring talented personnel to subsidiaries and affiliates with the intention of having them return to the parent company in the future. This not only enables NTT to operate efficiently and flexibly as a whole, but also will facilitate effective use of the available in NTT's labor force as well as generally contribute to the activation of the whole enterprise.

The law stipulates that the mutual employee welfare framework of NTT is applicable to new NTT affiliates (enterprises funded by 25% or more NTT capital, or consisting of 50% or more (NTT personnel), provided that suitable applications are approved by the Minister of Finance. Accordingly, personnel transferred to these enterprises by NTT will continue to receive the same benefits as regular NTT employees in such areas as pension, medical support, etc.

---

## **8. Changes as a Result of Privatization**

---

Privatization has had two major effects in the financial area: (1) release from budgetary control, and (2) termination of special treatment by the government. Item (1) is a big plus since it means that a check on NTT maneuverability has been removed. Item (2) means quite the opposite since the government will no longer be extending the support and protection it did when NTT was a public institution.

### **8.1 Release from budgetary restraints--facilitating mobile and flexible funds procurement and operations**

When NTT was a public corporation, limits were set every year on fund pro-

urement and debt redemption. Even when internal funds rose above the budgeted figure as a result of implementation of various revenue increasing and cost reduction measures, it was impossible to shift this money to use in reducing debts. In the new, privatized NTT, however, this type of restriction has been removed, thus facilitating freer maneuverability.

The need for approval by the Minister of Posts and Telecommunications every time it was thought desirable to float a bond issue or take out a loan has, moreover, been removed. This also needs dictating by NTT's flow of funds.

Further, it will no longer be necessary to deposit surplus funds in the national treasury, thus allowing freer financial operations. Deposits for payment, etc. will thus in the future be made in city and regional banks, further increasing convenience.

### **8.2 Termination of preferential treatment by the government--results will be determined by NTT's strengths and performance**

Since NTT is no longer a semi-governmental institution, it is no longer possible to make use of treasury investments and loan support based on Trust Fund Bureau and postal fund resources. Because of governmental guarantees, NTT's credit ranking when taking out external loans has been a high AAA. With the removal of these guarantees, however, it will be necessary to earn a new ranking on the basis of NTT's actual financial status. In other words, if NTT's fiscal status is good it will be possible to arrange loans at low rates. If, on the other hand, NTT's current condition is unfavourable, the cost of external funding floatations will be high. In conclusion,

NTT's financial base will have to be more solid than it has had to be in the past.

NTT has, moreover, been exempt up to now from fees for remittance of funds, etc. in its role as a semi-governmental organ. These will, in principle, also have to be paid

with the switchover to a privatized basis.

*As has been discussed, privatization carries with it both the plusses of a release from regulation and the minuses of a removal of protection.*

