

EICTA¹ Comments on the “Draft joint ERG and Commission Services approach to remedies under the new regulatory framework”

EICTA is concerned that the ‘draft joint ERG and Commission Services approach to remedies under the new regulatory framework’, hereafter referred to as the ‘Remedies Paper’, includes elements and trends that risk hindering the development of the communications sector in the EU. We feel that the thinking underlying the paper is too much premised on a static view of technologies and markets, and therefore risks discouraging investment in new technologies, services and networks. Furthermore, we note that the scope of the paper goes beyond remedies, and therefore have adjusted our comments accordingly.

The ‘Remedies Paper’ tends to favour an interventionist approach, inconsistent with the regulatory framework and likely to hinder innovation and investments in particular in emerging markets.

The ‘Remedies paper’ fails to establish a clear policy line. In some sections, the document rightly highlights the need to ensure incentives for investment and recognizes the very dynamic and unpredictable nature of electronic communications markets, but elsewhere it entertains interventionist ideas such as ‘assessing the economic desirability of duplication of networks’, or consider imposing retail price regulation on services other than those included in the Universal Service Obligation². In many occasions the document encourages the NRAs to impose retail price regulation - sometimes even below cost³.

1. EICTA welcomes the attempt made to define the notion of 'emerging markets' but we believe that this definition is incomplete and not sufficiently clear';

EICTA welcomes the statements that (section 3.3.2 page 71); “*when an NRA has outlined a genuinely emerging market that uses completely new infrastructure the approach is very simple: the NRA should let market forces work and not intervene*”; and (section 3.3 page 70) “*any potentially abusive conduct in the emerging market will normally be dealt with under standard competition law*”.

¹ EICTA, the European Information Systems Communication Technologies and Consumer Electronics Association, combines 46 major multinational companies as direct members and 31 national associations from 22 European countries. EICTA represents more than 10.000 companies all over Europe with more than 1.5 million employees and revenues of over 190 billion Euro

² The last but one paragraph on page 15.

³ The last but one paragraph on page 16.

Taken together, these two statements would provide a good starting point to develop a clear policy and set the basis for on-going investments to new services and networks.

However, the definition of the notion of an emerging market is a complex issue. First of all it is important to confirm that emerging markets are exempt from any ex ante regulatory obligation. It would thus be appropriate to consider them in the context of the periodic analysis of relevant markets prior to the discussion about ex-ante remedies and exclude them from any discussion on SMP designation and regulatory obligations.

Secondly it is important to clarify the criteria that will allow emerging markets to be identified as such. As shown in the section below, the new multimedia world makes market definition a complex and uncertain matter. Furthermore, and in particular if considered from a demand substitutability point of view, it would be difficult to find a new service that would not be to a large extent a substitute of an existing one. Broadband service provided over a completely new network, for example, fixed wireless, satellite or fiber optics would seek to provide services that were equivalent, yet perhaps more advanced or sophisticated service, than existing broadband offers. It would be the aim of an operator building this network to offer a choice (substitute) to existing services.

This is why we consider it particularly important to establish some clear principles establishing what can safely be considered as an emerging market. As correctly stated in the Remedies paper, emerging markets often involve sizeable and risky investments. It is thus critical for potential investors to have a clear picture of the regulatory implications. In our view, emerging markets are typically characterized by: a) innovation providing additional functionalities; and b) reliance on investment into new networks or significant network elements.

Furthermore and as already mentioned earlier in this paper, we believe that under no circumstances regulation should be extended into emerging markets. If there is risk of leveraging a significant market power to an emerging market, the problem should be addressed at its core, namely the relevant mature market where significant market power is being held and not at the emerging market level regardless of whether they are being provided over legacy network elements or not.

2. EICTA proposes the following approach when identifying emerging markets based on new services.

EICTA believes it is crucial to consider carefully any policy based on technological developments given the dramatic change in nature of the communication services made feasible (by widespread deployment of broadband.)

Comment:

In all broadband-based markets, the same end-user device can integrate voice, data, image and moving picture in its content functionalities. The same “communications link” can integrate voice, data, image and moving picture signals. The same “communications service” can contain any mix of access to and interaction with any type of content. Moreover, operators bundle different service components delivered previously through different infrastructures (e.g. Fixed and mobile, broadcast and telecom etc.) Consumers, on the other hand, can now have much more control over service selection, reception, performance and profiling. This allows personalizing a large number of end-user services and product features and potentially reducing the role of communication intermediaries (access operators, service and content providers).

One concrete example of such new multimedia services would be the “triple play” offer which combines voice, high speed internet access and TV or Video broadcast. Another example would be converged services over any delivery platform (new mobile content retrieved via both mobile and/or fixed end-user devices).

From a regulatory perspective new services can only be considered using “non technical criteria” such as: how the new service is put to market (bundled offer, integrated offer, multi-service basket, prime or discount service QoS) with reference to:

- a) the pricing model and its variants (unified or detailed billing, revenue sharing, retail-wholesale);
- b) who ‘owns’ the service subscription (shared or exclusive subscriber profiles, billing management);
- c) the relation between sub-service components as independent market products (e.g. VoIP integration in multimedia calls).

Any analysis of such new markets also needs to take into account the increasingly powerful and dynamic role of the users in this new multimedia and convergent environment. End users can increasingly 'zap' in real time among various types of services often provided by different service providers who in turn can also alternate between transport or access operators.

It is also important to note that the market for these new services and products is characterized by three critical factors:

- a) the need for extensive field trials and pre-marketing investments;
- b) higher costs for customer acquisition, complex billed billing, customer care;
- c) the phased and multidirectional nature in the new service penetration schemes over existing electronic communication networks.

Some immediate consequences for new services include:

- new services must be in the fully deregulated domain; we cannot imagine any new end-user service being subject to ex ante regulation;
- there is a need to distinguish (and exclude) content from transport when identifying a new communication service;
- there is a need to carefully assess whether new service components can be 'unbundled' by the end user to access alternative competing offers, and/or billed separately within the same subscription.

Finally, the need to recognize and measure the extent to which today’s regulatory uncertainty regarding how such new services can form emerging markets should become a short term priority for both the Commission and the NRAs if we are to avoid deterring investment in service innovation and R&D.

3. We would recommend the Remedies Paper to distinguish between old and new investments.

Undoubtedly, parts of the value chain of the communications industry present oligopolistic features. It is widely agreed that parts of the local access networks cannot be replicated by several operators in a commercially viable manner. On the other hand the deployment of such networks requires huge amounts of investment before any

revenue is generated. However, and as mentioned in the Remedies Paper itself⁴ ‘competition policy takes a much more benign view of market power that is caused by innovation....In these cases a balance has to be struck between preserving the incentives to invest and innovate (which will deliver higher growth rates) and the interest that consumers have in greater competition today.’

EICTA also believes that a relevant test for regulators would be to assess whether the ‘alleged restriction of competition’ would have occurred if the operator in question had not made the initial investments. In other words, in the absence of these first investments, would there be any market at all? If not, how can we accuse an operator of creating restrictions in a market that would not have existed in the first place if it had not been for its investments?⁵

EICTA would urge the ERG and the Commission to take all measures necessary to encourage the emergence of multiplatform access networks in Europe.

EICTA believes that platform access competition needs to be actively encouraged. A lot of empirical evidence from Europe and elsewhere proves that access platform competition is the biggest driver of innovation, broadband deployment and broadband penetration. This is why we believe that in cases where multi-platform competition exists, regulation needs to be held back, and this should be recognized explicitly in order to create sufficient regulatory certainty within the investment community.

4. The Remedies paper urges regulators in several sections to make an assessment on the ‘economic desirability of duplication of networks’ or to consider ‘the potential of inefficient investment’.

EICTA believes that Regulators should not make such assessments. The full liberalization of communication services and networks should mean that these decisions are left to markets. We cannot see how after full liberalization it can be the Regulator’s job to decide as to whether there should be one, two or several networks in a specific country or area. Furthermore, and as correctly stated in the ‘*Remedies Paper*’ itself, ‘*in a dynamic innovation driven market with the constant potential for disruptive technologies emerging, it is often impossible to predict with any degree of confidence the likely direction the market may take*’⁶

This is why we endorse the recommendation made a few paragraphs later in the same section where the Paper urges the NRAs to *be careful not second-guess the market place but rather to provide a coherent background against which market developments take place*’ In our view this phrase articulates in the best possible way the role of a NRA. An NRA shall not guess the future of the markets or to predict investments – it would be impossible anyhow.

We do appreciate that there may be occasions where an NRA has to assess whether the duplication of specific network elements may be commercially viable. Assessing whether the duplication of network is ‘commercially viable’ is a completely different matter to that of assessing the ‘economic desirability of duplication’.

⁴ Remedies Paper, Section 3.3, page 70

⁵ The investments required for deploying or upgrading a telecommunications infrastructure can be easily compared to the investment required for developing a commercially successful patent. IPR policy may have some interesting lessons for communication regulators who would like to encourage sizeable investments in new infrastructure.

⁶ Remedies Paper, paragraph 3.2.3, page 62.

5. EICTA believes that the Remedies should target the core of problem and not 'the consequences' in particular with regard to vertical leveraging;

Vertical leveraging is a risk in the telecom sector. However, we believe that the problem needs to be tackled at its roots, namely at the level of the value chain where market power exists and not in downstream markets. We are happy to acknowledge that the Remedies Paper includes a similar recommendation: '*NRAs can then apply the available remedy... that most clearly addresses the core of the problem*'⁷.

EICTA has always supported unbundling of the copper local loop that was built over decades under monopoly rights. However, we are wondering what is the 'high and non-transitory entry barrier' for a new entrant to provide broadband services to end-users once the local loop has been unbundled.

We do appreciate that the unbundling of the local loop does not remove the need for capital investments in order to offer broadband services (backhaul capacity, servers and routing equipment etc), as well as significant operational expenditure (marketing, operations, personnel etc.). However, a need for investment cannot be possibly considered as a 'high and non-transitory entry barrier'. Entering any business, in particularly a dynamic network business, requires significant investments that must happen without clear visibility into demand of services and bear therefore a significant amount of risk. The mobile networks are an obvious example of such investments – no one was able to predict the surging demand, but the investments had to be made before it became apparent. **Risk is not a 'high structural barrier to entry' and definitely not a 'non transitory entry-barrier'; it is an inherent element of a market economy.**

The above notwithstanding, efficient implementation of the unbundling of the local loop remains a basic prerequisite for opening competition in the access market.

We question the theory about assisting operators to climb the 'investment ladder'. We wonder why an operator would continue adding steps to this ladder if these new higher steps in this ladder will have to be shared with the competitors.

6. EICTA would like to seek clarifications regarding the statements included in the Remedies paper whereby the NRAs may impose remedies based on the incentives an SMP company may have to behave in an anti-competitive way⁸.

In EICTA's view imposing remedies based on 'possible incentives' could be dangerous. First, such a statement could be interpreted as asking the regulators to make assessment of future development of a very dynamic innovation driven market and the role players are likely to hold in this context. Secondly, such a statement would seem to ignore that SMP operators – despite their inherited market power- are mostly privatized companies that operate at the conditions of market economy; they have to make profits and yield a return to their investors. This is why we believe that some further clarification is required with regard to these statements.

It is our belief that a main objective of an NRA should be to introduce mechanisms that would allow monitoring the market efficiently in order to prevent abuses and to create positive incentives for operators to behave pro-competitively. If operators know that their behavior is being monitored in an efficient manner, they are very unlikely to attempt to abuse their position and risk fines etc. Effective monitoring of the markets is likely to deter operators from abusive behavior as much as intrusive regulation but without the adverse side effects.

⁷ Remedies Paper Section 3.2.1. page 59

⁸ Section 4.1 page 75 last paragraph.

Conclusion

Ill-conceived regulation can have a chilling effect on investments. As Jerry Hausman has shown⁹, a telecommunications company, like any other company, makes a large number of investments in many new services and products. Some of these new products and services may prove slow to market or unsuccessful. If the returns on the successful investments are regulated to the cost of capital, how will the operators pay for the unsuccessful projects?

Moreover, EICTA requests that the section on emerging markets be dealt in more depth in a separate document after close consultation with industry.

We hope you will find these comments useful. We remain at your disposal for further clarifications.

⁹ *Valuing the effect of regulation on new services in telecommunications* Jerry Hausman in Brookings Papers on Economic Activity, Microeconomics Volume 1997 (1997) 1-38