

ATUG Opinion – 5 December 2007

ATUG attended the 8th European Competitive Telecommunications Association Regulatory conference. A number of topics of interest to ATUG were discussed: Universal Service, the European Framework proposals; Investment in Telecoms; Functional Separation; Next Generation Regulation; Mobile Services and Fixed Mobile Convergence, Liberalising Spectrum. This week's Opinion looks at the range of views on Functional Separation.

European Commissioner for Information Society and Media, Viviane Reding spoke to the proposed new remedy, Functional Separation:

“We must accelerate our regulatory efforts in areas where competition has been slow and where persistent bottlenecks remain. If we just have a look at direct access competition in Europe – an area which is, to some extent, also crucial for the development of broadband – only 10.5% on average of the market is today in the hands of alternative providers which provide their services via their own network, via cable lines, unbundled lines or wireless access. 89.5% on average of direct access is however still dominated by legacy providers, the former incumbents. This means that ex-ante regulation continues to play a crucial role in maintaining competition and protecting consumers by setting conditions for access to the incumbent's infrastructure.

Assuring such equivalence of access can prove difficult where network operators are vertically integrated service providers, especially as regards non-price discrimination. **In cases where such discrimination is persistent and cannot be resolved by behavioural remedies, functional separation would remove incentives to discriminate between service providers. That is why the Commission proposes to provide the national regulators with the power to impose functional separation as a new remedy tackling persistent discrimination.**

Functional separation entails changes to an incumbent operator's organisation and incentive structure, including setting up information barriers between the access and services part of the business, but it does not force the operator to sell off assets. This is a proportionate and flexible approach tailored to the circumstances of the telecom sector. It is not superimposed where it is not needed and other remedies would be sufficient. But, where the opposite is the case, where the existing remedies are insufficient, how can we be satisfied with that situation? That is why independent regulators need this extra tool of functional separation where there are persistent structural competition problems.”

Lord David Currie, Chairman OFCOM spoke about the UK's experience to date with Functional Separation:

“Two charges are laid by opponents of functional separation. First that it is costly and bureaucratic; secondly that it deters investment. Let me deal with both in the UK context. Functional separation has, of course, had some transactional costs for BT. But, as they recognised early on, it can also bring them benefits.

As regulation focuses on the business unit that manages the natural monopoly assets, the rest of the Group can think like, be managed like and run like a competitive international-focused PLC, not a regulated business hamstrung by intervention.

And as regulator we can step back increasingly from regulation, both at retail level where we ended price regulation 15 months ago and increasingly at wholesale level. We are currently consulting about deregulating wholesale broadband in newly-competitive sub-national markets. And we expect to announce further deregulatory measures in the coming weeks.

As to investment, the relative performance of BT's share price both in the UK market and by comparison with Continental peers, suggests that the UK's approach has not troubled the capital markets.

Nor has it constrained BT's ability or appetite to undertake efficient investment. It is currently embarked on a 15 Billion Euro programme of investment in its next generation core network.

“Efficient investment” are the key words when it comes to Next Generation Access too.

It should be no part of a regulator's brief to secure investment for its own sake.

Misdirected or premature investment leads to allocative inefficiency in the wider economy. Rather, the regulator's job should be to enable investment when a competitive market is ready for it and to ensure that there are no perverse incentives in the way which artificially constrain new investment.”

Grant Forsyth of BT gave the conference an update on BT's views of Functional Separation debunking “The Myths of Functional Separation”. Forsyth will be providing an update of this presentation at ATUG 2008.

- “1. Destroys the efficiency of vertical integration
Where is the evidence that a vertically integrated incumbent is efficient?
2. Suppresses investment
Greater certainty supports wider investment from incumbent and entrants
3. Suppresses investment in fibre
UK committed to green-fields FTTP on an EOI basis – no “Regulatory Holidays”
4. Creates a monopoly
Entrants free to invest where opportunities exist / business case works
5. Duct sharing is a better alternative
How is equivalence of access to be delivered? FS?
6. Replicability is a better alternative: Equivalence = Equal
7. Too costly
To whom? Costs of competition always “too costly” when imposed
8. Destroys the share value of the incumbent
Not the experience of BT”

Richard Cadman presented the 2007 ECTA Regulatory Scorecard addressing the particular issue of the positive effect of competition on investment and innovation:

“ECTA's latest benchmark of 19 European countries shows the lowest prices and highest investment occur where regulators have strong tools to enforce EU pro-competition rules. The 2007 Regulatory Scorecard is (a) report, commissioned by the European Competitive Telecommunications Association (ECTA), (which) compares the telecoms regulatory environment and the application of the current legislative Framework in 19 European countries. This year's results show that countries where regulators have taken action to enable competition to flourish, including the UK, Netherlands and Scandinavian countries, have seen strong performance in their telecoms markets. However, others including Poland, the Czech Republic and Greece have fallen behind, while institutional weaknesses may be preventing Germany, Belgium and Finland from reaching their full potential. The 2007 Scorecard also clearly illustrates that the ability of the regulator to tackle competitive problems can have immediate and tangible consequences for consumers – affecting the price of telecom services, as well as affecting longer term investment in the sector. In particular, in countries where regulators have enforced access to the incumbents' local loop to open broadband markets to competition, broadband prices are typically the lowest and the broadband speeds the fastest.”

The Scorecard (188 pp) is at http://www.spcnetwork.co.uk/uploads/Regulatory_Scorecard_2007.pdf

Next week's Opinion will be an update from the users' point of view from the INTUG December meeting.