FREE NETWORK
POLICY BRIEF SERIES

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April 2018

Focus on Investment: a Brief Look at Regulatory Developments in EU Telecommunications

The European Commission recently proposed a revision to its existing regulatory framework for telecommunications, the details of which have been amply discussed and are currently being negotiated. A pivotal theme of the revision is a stronger emphasis on stimulating investments into broadband networks capable of delivering high-speed (100+ Mbps) internet services. This brief highlights and briefly discusses some key changes in that regard.

Introduction

High-speed broadband networks are the backbone of the fast-growing digital economy. Promoting citizens' access to such networks has been one of the European Commission's stated policy priorities at least since 2010, when it launched its "Digital Agenda for Europe" (EC, 2014). Its policy mix of choice involves measures and funds facilitating deployment of so-called next-generation access networks on the one hand (commonly taken to mean access networks capable of delivering speeds exceeding 100 Mbps), while on the other hand regulating access to such networks to the extent perceived necessary to deal with potential problems resulting from incumbent network operators' degree of market power. As regulation may harm incentives to invest in network infrastructure in the first place, a balance between investment promotion and competitive safeguards needs to be struck.

Motivated by what it considers to be a sub-optimally low speed of network upgrading in at least some of the EU's member states, the Commission has sought to adjust its policy balance in favor of investments by proposing a revision (EC, 2016) of its regulatory framework for electronic communications, called the European Electronic Communications Code (EECC), which defines a standard approach to regulating fixed broadband network operators deemed to possess significant market power. That revision has been commented upon and discussed by the European Parliament and the European Council as well as various private and public stakeholders (Szczepański, 2017). Several amendments have been proposed and further discussion is ongoing to reach a compromise between the European institutions.

Background

Telecommunications networks were until more recently typically owned by vertically integrated, often formerly state-run, national incumbents who even after their privatization and the elimination of most legal barriers to entry were considered to possess significant market power. The EECC's key remedy to such market power is so-called network unbundling at the wholesale level: considering the retail market for internet service provision potentially competitive, unbundling means granting competing internet service providers regulated access to the incumbent operator's physical local-area access network, which is commonly regarded as the key bottleneck in internet service provision. Choosing the intrusiveness of the access obligation is up to the national regulatory authority (NRA), ranging from merely demanding that the incumbent publicly post a reference offer, to stricter measures such as non-discrimination, "fair and reasonable" pricing, and ultimately, full-on access price regulation, typically implemented with price caps derived from regulatory costing models. A recommendation from 2013 (EC, 2013) outlines methodological guidelines to national authorities.

Key changes

The proposed EECC revision makes the abovementioned recommendation binding, which may partly be an attempt to further harmonize regulatory practice between member states, with a view to encouraging cross-border investments by operators and service providers. It also encourages NRAs to, where possible, abandon more rigid price regulation in favor of margin squeeze tests. Margin squeeze occurs when a vertically integrated firm with market power in the wholesale segment of a production chain "squeezes" retail competitors by setting high wholesale and low retail prices, to the extent that even equally efficient, or at least reasonably efficient, retail competitors cannot survive if they are dependent on the dominant firm's wholesale product. Moreover, and more importantly in terms of boosting deployment, the proposal encourages lighter-touch regulation for operators deploying new network infrastructure (Art. 72), and specifically relaxes regulation for deployment projects open to co-investments between operators (Art. 74). It also extends the market review period, i.e. the frequency at which NRAs are expected to update their market analysis and regulatory policy, from three to five years, giving operators a longer planning horizon, and encourages NRAs to consider any existing commercial wholesale offers in their market analysis, which can be interpreted to mean that anything short of full market foreclosure should be looked upon benevolently (Articles 61 and 65). In line with this latter development, which suggests a focus on wholesale access *per se*, is Article 77. This article exempts so-called wholesale-only networks – non-integrated networks whose very business model is selling access to interested internet service providers – from strict access price regulation, at least *ex-ante*. Typically, a presumption of consumer harm absent regulation is sufficient for intervention. Article 77 turns the tables on regulatory authorities by requiring evidence of actual consumer harm.

A counterpoint to these deregulatory elements is Article 59.2, which under certain conditions not only allows but obliges NRAs to impose access obligations on owners of existing physical infrastructure "up to the first concentration point", in practice affecting mostly in-building wiring and cables, even when these owners have not been identified as dominant in any relevant market. In countries such as Sweden, where in-house wiring is often not owned by any operator but rather by the respective building's owner(s), implementing such obligations may pose a regulatory challenge.

Finally, Article 22 requires NRAs to chart existing infrastructure as well as deployment plans across the country and enables them to define "digital exclusion areas" where no high-speed broadband infrastructure exists or is planned. In such areas, they may organize calls for interest to deploy networks, also with a view to resolving potential coordination problems between operators resulting from so-called "overbuild risk": deployment in some lower-density areas may only be profitable if most of the customer base in that area can be captured, leading to a standoff between operators who cannot, do not want to, or are not allowed to communicate and coordinate their deployment strategies. As a result, investment is delayed.

A rather piquant detail here is that the proposed code allows NRAs to take action against operators it suspects of "deliberately" providing "misleading, erroneous or incomplete" information about their deployment plans. Included to prevent gaming, this provision carries the risk of suppressing investors' appetite for the designated exclusion areas lest they be punished in case they change their mind. A minimum of mutual trust between the national regulator and market participants seems crucial for this mechanism to succeed.

Conclusion

The Commission's proposed new regulatory framework emphasizes investment in, and take-up of, high-speed (100+ Mbps) broadband networks, explicitly defining such enhanced connectivity as a new regulatory objective on equal footing with the existing ones, most notably the promotion of competition. The present brief points out some key regulatory changes aimed at the fulfilment of these respective objectives. In terms of the revision's impact on high-speed broadband deployment in the EU's member states, it is difficult to make a general prediction since Europe is somewhat heterogeneous with respect to high-speed broadband penetration. For example, the 2016 EU overall NGA coverage was 75.9 % of households, but coverage rates of individual countries ranged from 99.95 % and 99.86 % in Malta and Belgium respectively to 47.0 % in France and a mere 44.2 % in Greece (EC, 2017). To the extent that the new code encourages investment relative to the old regime, regions with lower current coverage stand to benefit more. To the extent that the lower pace of deployment in those areas is the result of other factors orthogonal to regulation (one example being demand uncertainty), it will have a limited effect.

References

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