

---

# EU proposed telecoms regulatory changes: good politics, bad economics

October 2013

James Allen

---

The European Commission (EC) released *Connected Continent: Building a Telecoms Single Market* on 11 September 2013, a proposed legislative package that it stated is aimed at “building a connected, competitive continent and enabling sustainable digital jobs and industries.” This may be good politics, but it is not good economics. Lower prices may be popular today, but if they are inefficient they will lead to lower investment and this is bad for consumers in the long term. This article examines the key points of interest from the package.

## Mobile

The EC is seeking a long list of major changes in the mobile market, including:

- the removal of charging for incoming calls while roaming in Europe
- net neutrality, so removing the ability to charge a premium for access to certain (Internet-accessed) applications
- either ‘roam like at home’, or decoupling (a roaming solution already planned to be implemented in 2014, enabling the purchase of roaming services from a third-party provider)
- the removal of almost all of the premium for international calls within Europe (though the detail suggests that price elasticity is an acceptable justification for higher prices, making this essentially just posturing)
- working towards improved harmonisation of allocations and allocation timescales for future spectrum releases (which would be good, but we believe is a very long-term aim and in fact unlikely to be achieved).

All bar the last would be materially negative for mobile operator margins if they occur.

The roaming proposals are likely to lead to the offer of decoupling (which we already knew about) as being less negative for operator margins than ‘roam like at home’, at least in the short run. ‘Roam like at home’ has specific difficulties including material arbitrage risks if the wholesale offers are at low prices. The wording of the proposed regulation allows wholesale agreements preventing this arbitrage, but achieving such an agreement while remaining compliant with competition law may be difficult to achieve. However, the ability to implement ‘roam like at home’ and stop offering decoupling may itself deter serious investment by parties wishing to offer decoupling.

### Efficient pricing

The Commission appears to be arguing that because the underlying costs of providing roaming (and international) calls are not that much higher than national calls, prices should be similar. This is not efficient, because operators know that consumers are more price sensitive for national calls. Forcing the price of national and roaming calls to be the same means that operator revenue will decline even if, as is almost inevitable, the operators increase the price of national calls slightly to compensate for the loss in margins (a ‘waterbed effect’ – which may not be complete). Higher prices for national calls will slightly reduce demand – and recover lower total revenue than a situation with high roaming charges. Ultimately, anything that reduces total returns in the industry is bad for investment.

The contrast with the device market is quite striking. iPhones do not have a removable memory card slot, and Apple charges a substantial premium for models with higher memory. Apple does this because consumer preferences allow it to: it makes more money with that pricing structure despite the manufacturing and marketing costs being very similar for both models (it is ‘allocatively efficient’). This is analogous to the higher prices for roaming calls that the Commission does not accept.

## Fixed

In addition to net neutrality and (perhaps) removing voice premiums for international calls in the EU, the package also includes a number of specific proposals on fixed networks, in particular in relation to creating common wholesale products across the EU. Difficulties here are likely to be practical, involving changes to the nature and interfaces of the wholesale products used by ISPs (such as the current local versions of fibre-based wholesale products) in all 28 countries. These changes and difficulties will introduce as much uncertainty in the medium term (in order to create these new products and migrate to them) as the policy aims to remove in the long term. It will certainly be a challenge to encourage investment by alternative operators planning to buy the existing wholesale products in the interim until this significant uncertainty is resolved; as a result incumbents and cable operators will probably make net gains in the short term.

## Changes to the regulatory framework

The Commission is also keen on a ‘passport’ scheme to allow an operator to be authorised to operate in any EU country and to make it more common for end users to buy services from telcos established in other member states. However, wrapped up with this is a right to equal treatment by the different member states in objectively equivalent situations, enforced by the Commission – which would thereby obtain a veto on national regulatory decisions. This is a power it was specifically denied in negotiations over the 2009 package, which will be contentious. The right to equal treatment goes towards centralising regulatory decision-making (at least as regards what the appropriate remedies are in ‘objectively equivalent situations’) – though not yet a single European regulator. It is apparent that the Commission still desires this level of centralisation as an end goal.

The regulation also creates the possibility of dispute resolution across borders (a dispute between BT and Orange about some matter in France could be resolved by Ofcom in the UK, albeit taking ARCEP views into account). This is surely impractical for a multitude of reasons, unless the regulator of the country concerned (ARCEP, for example) makes the decision and this is just approved by the host country regulator.

These are only the highlights of the long list of proposals – there are plenty more. The combined effect is not positive for investment in networks, despite the Commission’s rhetoric – they characterise the proposals as “a mix of sweet and sour.”

Some of the proposals will probably be modified in discussion with the European Parliament and the Council (that is, the member states). Operators wishing to make a principled case against the proposals will therefore need to focus on these fora.