

EETT's 3rd International Conference on Broadband Internet

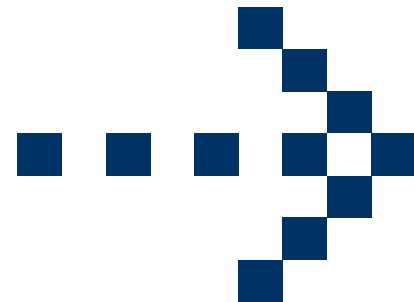
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'Innovative Regulation for Competition in
Broadband Markets - Separation'

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Terminology 1

Vertical vs. horizontal

‘Voluntary’ vs. mandatory

Where to separate: ‘Netco’ vs. ‘Loopco’ vs ‘3-box’

Terminology 2

Types of separation

Ownership
Legal
Functional
Virtual
Accounting

Examples to date

Horizontal

Divestment of cable/mobile etc

Vertical

Functional:

UK- Openreach

Australia

New Zealand

Italy

Sweden

Structural:

USA

Ireland

See: *IDATE, Functional separation in telecoms: panacea or plague?*
2008

Why do it?

Accounting separation can deal with vertical leveraging of price from monopoly to competitive segments (eg. margin squeezes), but non-price discrimination is more difficult

‘Sabotage’ can be profit-enhancing if:

- i) monopoly activities are regulated to cost
- ii) the retail market is homogeneous
- iii) the integrated firm is efficient downstream

What are the costs of separation (if more competition is the benefit)?

- ▣▣▣ One-off reorganisation costs
- ▣▣▣ Continuing costs of contracting
- ▣▣▣ Co-ordination costs
 - ▣▣ Operational
 - ▣▣ Investment

Sectoral parallels

Energy:

EC espouses unbundling to open up markets and allow international interconnectors

Railways:

some examples of flawed separation (eg. UK), others more successful

Postal services:

consideration given to separating/franchising local delivery segments etc.

The impact of integration- a literature survey

Empirical studies show that in most circumstances profit-maximising decisions are efficient AND benefit consumers

but, the risk of anti-competitive conduct is there

Lafontaine and Slade, JEL,2007, pp629-85.

What does functional separation entail in relation to investment?

No account to be taken of revenues generated outside the separated division

e.g. BT undertakings (5.13.2): ‘Any investment decisions shall be considered solely on their own merits and should not take into consideration the potential impact on other products...’

Does this make functional separation equivalent to structural in this respect?

How is investment in NGAs affected?

- ❏ In competitive markets, forbearance may be chosen- no need for separation
- ❏ In monopoly markets, an access regime will be necessary, and functional separation can be used to ensure/maintain equivalence
- ❏ But NGAs present a particularly significant investment co-ordination problem
- ❏ Also NGAs can be designed to discourage discrimination.

Can contracting solve the investment co-ordination problem?

- ❖ Information transfer can be accomplished by independent forecasting or constructive engagement
- ❖ Contracts can be long term and involve take or pay elements or other forms of risk-sharing
- ❖ Examples can be found in sectors such as airlines/airports, energy, railways and in activities of unregulated firms such as Intel (job 1 and job 2)
- ❖ But the question must be answered on a case-by-case basis.

Where are we now in Europe?- Voluntary separation

- ☒ Recognised as unlikely to be harmful; market power likely to be reduced and consumer and share holder interests can be aligned
- ☒ Proposal to require NRA to review regulatory obligations after such a separation
- ☒ This should lead to some deregulation

Where are we now in Europe?-functional separation

- ❑ this is a necessarily costly and intrusive measure which may be difficult to accomplish in the face of opposition
- ❑ it should be employed in the presence of evidence of failure of other remedies- ie only deployed if the goal of equivalence is not obtainable without it
- ❑ it should be a available subject to safeguards
- ❑ The commission's proposals strike a good balance.