



Office of the Director of
**Telecommunications
Regulation**

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to the

Institute of European Affairs

10 April 2000

**EU Liberalisation and its impact on National Regulation:
Telecommunications**

Document No. ODTR 00/26

10 April 2000

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Introduction

Chairman, Fellow Speakers and Panellists, Ladies and Gentlemen, it gives me great pleasure to address you today, and I would like to thank the Institute of European Affairs for inviting me to do so.

I have taken the liberty of altering the title of my speech from “EU Deregulation and its impact on National Regulation” to “EU Liberalisation and its impact on National Regulation.” The EU’s liberalisation programme for telecommunications (and the utilities in general) has involved the radical introduction of competition in a previously largely state-owned sector for the first time. I want to emphasise that this is an opening up of the market. To facilitate this opening up of the market, the EU has not decreed the disappearance of regulation; rather a rethink of its form.

State ownership was the traditional instrument for provision of utility services and was widely used throughout Europe, and indeed most of the world. The opening of parts or all of the market in telecommunications to private firms has required Member States to engage in regulatory reform, setting up new licensing systems and institutions to underpin the new markets. It has forced a re-think of the requirements for the provision of services, a re-think that has caused many countries to engage also in the privatisation of former state-owned monopolies as well as the liberalisation of national markets and the setting up of independent regulatory bodies. No longer are the needs of the incumbent the central focus of public policy – there has been a clear shift to the needs of users, and an understanding that effective competition provides the best guarantee of best quality and best prices. As competition grows and competitive pressures become strong enough to ensure that the market can sustain itself effectively, we will need an EU deregulation programme for the sector of communications. If we had already got there, I would not be standing here today speaking to you.

The purpose of my speech today is not only to assist, but also to encourage the IEA in the pursuit of its aim of developing understanding and debate and thereby influence EU policy making. In the context of communications (and other sectors where regulation and liberalisation have replaced the model of state-owned utilities), I see the IEA's objective as getting to grips with the current growth of regulation at EU and national level and to encourage and assist the Irish public and the telecommunications sector in particular in becoming more heavily involved in the consideration of EU affairs.

The Information Economy and Ireland's Competitiveness

The combination of rapid development in technology and global competition as well as major volatility in demand is driving significant changes in the way we do business and organise our work. In other words, the economic landscape is changing, from the "industrial age" where value was vested in tangible products to the "information age" where, as Commissioner David Byrne has aptly stated, knowledge and its application "becomes the new currency".

This transition towards the knowledge-based economy highlights the critical role of Information and Communication Technologies (ICTs) for economic development and job creation. ICTs are fundamental to continued economic development, providing the basic infrastructure for communications and movements of information. The communications and electronic commerce sector is already altering the *modus operandi* of our traditional industries, the organisation of work and the two-way interactions between business and consumers. The growth of such things as the Internet, the high-speed exchange of large volumes of information, videoconferencing and large corporate databases clearly illustrates the impact that advances in ICTs are already having.

This, in turn, highlights the fact that telecommunications policy is a key instrument in sustaining the economic development and competitiveness of our nation. IDA Ireland continues to market Ireland and its “Celtic Tiger” economy as an attractive location for new investment from overseas. A fundamental element in their success has been the ability to market highly developed national infrastructures. EU structural funds have contributed greatly to the transformation. The Department of Public Enterprise continues the drive towards increasing the stock of this infrastructure covering the country, and more particularly the stock of communications infrastructure through its broadband programme. Ireland has already invested US\$5 billion in telecommunications infrastructure over the past ten years. A further US\$700m is to be devoted to technological research alone over the next few years. Investment continues to grow, which has served and will continue to bridge remaining gaps between Ireland and our OECD competitors. The new Global Crossing development, in partnership with the Department of Public Enterprise, will provide a high-speed, high-capacity link to the US and Europe increasing 15 fold the current capacity. Leading edge companies with high-capacity requirements can be guaranteed connectivity, further enhancing IDA Ireland’s ability to attract foreign investment.

You may ask, given current levels of growth, why continue to prime the pump of high tech industry and telecoms? The speed of change is such that if Ireland does not continue to move along the leading edge, it could rapidly fall behind, and the current upward spiral could rapidly turn downwards, for the domestic market is too small of itself to be a major attraction to the type of company that form the engine of our economic growth. We have seen an explosion in indigenous companies in software, for example, but these are highly interdependent and dependent on the international giants. We should not lose sight of the need to maintain critical mass at the leading edge, even to retain the people who are at the forefront of these indigenous developments.

The development of a vibrant telecommunications sector, providing the best in price, choice and quality to users is essential to underpin our ‘Celtic Tiger’. So we need an effective regulatory regime to ensure that the sector develops as quickly as possible. The way the EU shapes its framework of Directives and other measures, the way the national Government transposes that framework and places it alongside a broader framework of promotion for the sector, and the way that my Office implements and details it determine the effectiveness of the regulatory regime.

I might note that telecoms development is essential for our economic prosperity, but it is also essential to social and regional development, for extensive advanced services are and will be ever increasingly needed throughout Ireland to support jobs and the people who have and want them outside of the main urban centres.

The European Context

What have been the driving forces of the currently observed “fashion” of regulation in Ireland? We were not alone in the traditional analysis that, due to the structure of costs, telecommunications was viewed as naturally monopolistic and, therefore, an industry where competition was not feasible. The traditional solution was state ownership. At times when it was rather more difficult than today to obtain capital for telecommunications development and when changes in technologies and demands came over decades rather than over months, this had some force, particularly in a country such as Ireland.

From the early 1980s onwards, things began to change. The realisation that much of the vertically integrated activities of network industries could be provided competitively led to regulatory reform in the US and the UK. In both cases, rather complex models of market opening were used. In the USA, the long distance and international markets were treated differently to the local one, while in the UK a duopoly was created initially. Both types of structures were complex and imperfect and required very heavy regulatory intervention, but even so, the experiments were successful in making some changes in prices and services, and further market liberalisation followed.

Also in the 1980's, the European Commission was looking with increasing disfavour on the state-owned and supported monopolies in telecommunications and in 1987 began a series of measures to open the markets, starting with equipment and then adding other areas. Like the UK and the US, there were concerns about full market opening, which in the EU took the form of the protection of the voice telephony markets to the incumbents, a last barrier that fell in 1998. Ireland, which had put in a huge effort to upgrade its telecommunications sector in the 1980's, did not however move with the leading countries towards liberalisation. The history will be written later, but it appears to me that there was too great a concentration on the perceived needs of the incumbent at the expense of the user, including both the major businesses on which our economic growth is heavily dependent, and also the ordinary consumer and small business user. Liberalisation may have been seen more as one of those prices that Ireland has to pay from time to time for the benefits of EU membership rather than a benefit in its own right.

However, finding ourselves at the back of the class in early 1998, we realised that such a position was no place for a country with not just aspirations but every intention of maintaining and developing our world class, high tech industrial base. We changed our minds and started a headlong process to catch up and move to the leading edge across the whole range of telecommunications policies. The May 1998 declaration abandoning the derogation to 2000 on full liberalisation confirmed the new direction. There has been a sharp decline in the prevalence of the view that liberalisation and competition are simply EU impositions to be endured and kept to the minimum possible. They are now seen as key enablers to ensuring the continued health of the nation.

Therefore, the most important driving forces of the current wave of regulatory reform and liberalisation in Ireland were the congruence of industrial development needs and the progress of EU liberalisation. We were fortunate that, with all its limitations, there was an EU framework there that we could pull off the shelf and adapt for Ireland. To have started the task from scratch would have taken far more time and resources.

Ireland is not alone in realising the importance of telecommunications as a key driver of economic growth. A headline conclusion from the Lisbon summit (23-24 March 2000) was the desire to set a clear strategic goal for the European Union for the next decade as follows:

To become the most competitive and dynamic knowledge-based economy capable of sustainable economic growth with more and better jobs and greater social cohesion.

Two important conclusions can be implicitly drawn from this strategic goal:

1. The emphasis on *knowledge-based economy* and the implied importance of the communications sector, given the discussion above;
2. The fact that the continued development of telecommunications is now a key competitive issue between the EU and competing continents, such as the USA and Asia.

It was very interesting to see the Summit seek to tackle these complex issues and I expect we may see more substantive decisions in this area in the future.

I will deal with the issues arising from the first in more detail later. As regards the second, we are already observing commentators and policymakers noting the state of the EU communications sector compared to the US. Globalisation is causing people to think globally, and so must we. The situation is often compared to a race, a competition between the two, but given Ireland's position we have every reason to make use of the valuable benchmarking that comparisons can give, but should seek to avoid the development of 'wars' of the kind that have affected products such as bananas and beef. Both the USA and ourselves are turning more clearly than ever to focussing on user needs. If we do so effectively, we should avoid wasteful conflict – and may devote more energy to helping others.

The statistics show that Europe lags the USA on Internet usage and on PC ownership. Recent surveys show that Internet penetration in the US is currently at 63%¹. Certain individual European countries can match this – notably Sweden with 60% penetration, but the European average is running at around 25%².

¹ Amarach survey

² NUA Internet

Ireland is estimated to have a penetration rate of 22%³. On the other hand, the EU is ahead in mobile penetration and in smart cards. Mobile penetration rates in the US stand at about 32%⁴. Compare this with Ireland's penetration which was 46% at Christmas, so I suggest may well be at the 50% mark by now and is growing rapidly. In terms of subscribers, Europe has 120 million subscribers compared to 79 million in the US and 46 million in Japan⁵. Internet businesses lose money on both sides of the Atlantic, but recent work by McKinsey suggests that European companies are losing less money than their US counterparts. Whether this will lead to real advantage remains to be seen. Differences in cost structures, in culture, in non-regulatory public policy objectives account for some of these, but it should be noted that regulatory differences may have contributed significantly also. Different technologies meant that the USA is not a "single market" for mobile the way Europe is and litigation following some auctions in the mid 1990s limited the number of competitors actually entering US regional markets for some years. In comparison, the maturity of the US market and its lower cost structures made cheaper Internet a practical possibility rather earlier than in EU markets.

Peter Sutherland recently remarked that "US business has recognised its vital interest in having a close connection with regulation which we in Europe have not developed to the same extent". He argues that there is a need for greater involvement by companies in the process of economic development. I share the view that there should be a consultation process to ensure that the operators do develop and make their views known on major regulatory change at the WTO as well as the EU. I believe very strongly that 'regulatory capture' does not make for good regulation in favour of the user, but it is important that regulators know and take account of the views and capabilities of the operators are in taking decisions.

Policy consistency on a global scale should be a priority if the vision is identical (which it should be), that is, working to improve the price, choice and quality of telecommunications services to end-users. The major IT and networking companies are largely US and have global reach. The EU should be aiming as high.

³ Amarach survey

⁴ US Cellular Telecommunications Industry Association

⁵ DG-INFSO

Decision-Making

What are the implications of all of the above? Telecommunications, as a consequence of Ireland's established membership of the European Union, has joined a long list of sectors where policy is now primarily formulated in the EU. It is only as the current review of the regime – the 1999 review – gets underway that the central role of the EU has come into sharper focus. To date, substantial attention in Ireland has focussed on the regulator. However, the regulator, the National Regulatory Authority in EU parlance is a creature of statute, domestic and EU. We operate within a tight framework of EU and national law, the EU framework being most important in terms of the range of regulatory tools, the national in terms of powers and structure of the institution.

Until recently, in telecommunications as in many other fields, Ireland has acted as a policy-taker in relation to the EU framework. We now have the opportunity to influence policy development at EU level. The Secretary General of the Department of Public Enterprise is well known for his work in relation to the EU approach in respect of e-commerce. There is now the opportunity to influence the whole regulatory framework for telecommunications, a task that falls centrally to the Minister for Public Enterprise and her officials, but which should also be informed by the views of the industry and consumers. My European regulatory colleagues and I believe that we have something useful to contribute on the basis of our 'coal face' experience.

Assessment of the Current Regulatory Framework

The DG Information Society started a review last year to prepare an overarching framework to oversee the transition to the knowledge-based economy that was spoken about in the strategic goal for the European Union at the Lisbon summit. Its policy objectives can be summarised as:

1. The promotion and sustenance of a competitive European market for telecommunications services;
2. To ensure continued benefits to the European citizen;
3. To consolidate the internal market in a convergent environment.

What can be said of developments to date? Firstly, amid all the clamour that accompanies any radical change in the status quo, let us review the current framework. It has achieved its basic aim – to open up the markets of the EU to full competition. There are many complaints that it has not done so fast enough or has been too fast, but the fact remains that the structure has done its work. The EU as a whole is not facing, as the USA faced after the 1996 Telecommunications Act, a series of long drawn out court battles that are only now coming to an end, which delayed the enactment of key elements of the provisions.

The EU regulatory package has been overtaken by the rapidity of technological and market change that it was designed to promote. These changes are numerous, but some of the principles ones are:

Convergence makes the traditional separation of regulatory functions between the communications, broadcasting and IT sectors increasingly obsolescent;

Globalisation of technologies and markets is raising technical, commercial and legal issues that require solutions of a global nature;

Mergers and Acquisitions are creating firms with the ability to operate not only on a pan-European, but also a global scale over new and expanded infrastructures;

Cross-border problems are increasing as the previous two developments continue to grow and the traditional national boundaries of markets continue to fall;

The Internet and its continued expansion is making redundant traditional views of market structure and blurring the distinction between voice and data transmission services by providing a common platform for the delivery of wide ranges of services.

The current regulatory framework was not designed to cope with these changes and its shortcomings have already emerged. The EU market has grown out of its initial framework – the market needs more space to move on, and in particular needs to be relieved of its technological straightjackets. It needs to be simplified and harmonized and co-operation between countries needs to be strengthened and made effective.

Differences in treatment of voice telephony, data and leased lines, completely separate regimes for mobile and fixed telephony no longer make sense and need to be reviewed, although it is easier to say this than actually to get it all done. It is also clear that 5 Directives would make it easier for everyone involved with regulation rather than the current 23, again no easy task, but time does not permit me to go into detail now. I propose to concentrate on two issues, firstly harmonisation between member states and secondly the trigger mechanism for imposing substantial regulatory constraints on companies, to outline the issues and some suggestions as to how they might be dealt with.

National Differences – good subsidiarity or poor harmonisation?

Firstly, there are significant differences between Member States. National markets are developing from very different starting points and national perspectives and the degree of flexibility in the means and methods of transposition of EU law into national legislative frameworks means differences are to be expected. Now that the EU market has been opened, market pressures are moving pricing and products closer in all countries. For example, interconnect rates varied very considerably in the EU's first benchmark survey, with the prices in some countries a multiple of those in others. The most recent survey now shows substantial 'bunching of prices' close to the bottom of the range. All countries have licensing regimes based on the EU Licensing Directive, although there are many differences within these regimes, reflecting different traditions of licensing in different Member States and also the national legislative framework within which NRAs were established. In Ireland we have simply a two type licence regime, with the longer of the two running to no more than 40 pages. It would not be conducive to the development of the Irish market to have the full range of categories considered necessary elsewhere. You will all be aware that one EU country after another is arranging competitions for third generation mobile, in accordance with EU requirements, but dealing with national issues in respect of roll-out and other national obligations.

Where Member States fall behind in their obligations, the Commission has become ever more vigilant. Recently it started infringement proceedings against 6 Member States for failing to implement carrier pre-selection on 1 January this year. Ireland was not among the six.

There are differences between approaches between Member States that could be reduced to the benefit of users and convenience of operators, and co-operation across boundaries would ease problems of international trade in telecoms. Regulators have been aware of this for some time and set up an informal group to exchange views and seek to resolve issues. This group – the Independent Regulators Group – comprising independent regulators from all EU States plus a few others, has not been formalised. Although NRAs are responsible for the on-the-ground implementation of the EU's framework, they have not to date been given internal market or cross-border mandates. It has, however, been a very valuable forum for exchanging views and advice. It has a strong spirit of co-operation, and I, as regulator in a small country that came a little late to liberalisation, would like to place on record my appreciation of the work of the IRG.

The Commission has proposed a new institutional structure in which the NRAs would participate with representatives of other regulatory bodies and the Member States representatives in a forum to discuss high level principles and also some very detailed issues. In its response to the Commission's consultation the IRG has made the point that we would of course wish to be part of any such group, but that we feel it is impractical for very detailed issues. We have experience of day to day operation of regulation that we would wish to share with the Commission and look forward to proposals that might be made to realise this. Like the Irish navy on the Birmingham building site in the 1950's, we are best placed to say in respect of a faulty foundation wall – this lot is back-to-front - before it is concreted into new law or guidelines.

There is also a need to provide for cross-border competence for regulators if they are to tackle cross-border issues effectively. This is becoming increasingly important as markets become more and more global in nature.

The idea of an EU regulatory authority has not gained currency – it is seen as too complex, too institutional a solution, which would absorb all the energy of the policy making bodies to the detriment of other urgently needed changes.

Significant Market Power or Dominance – a debate for experts or key policy?

In its 1999 review, the Commission leaned towards the view that it should see the liberalisation of telecommunications completed relatively quickly and a move towards increasing reliance on competition rather than sector regulatory law within the likely period of implementation of the new Directives. NRAs have discussed this, and it is clear that some markets are more advanced than others, and some are more advanced in very specific areas than others. The danger of moving too fast from a regulatory regime to competition law alone for those who are behind the leaders, is that they would never catch up. Without regulation to support new entry, their markets would harden and fall back into monopoly or oligopoly, with all the attendant problems of high prices and slow adoption of technology which that is likely to bring. Accordingly, in the IRG response, we suggested that NRAs be given a tool box of measures to adopt depending on the circumstances in their own market, a tool box out of which certain items could be discarded once it was safe to do so.

This is by way of background to a key issue about which operators carry the responsibility of providing access to their networks at cost-oriented prices. This issue is a key principle for the opening of markets. The current EU framework provides for the concept of significant market power, which is set at 25% of specified markets, and subject to certain conditions. It is a new concept and all regulators have worked it through into the market. It has not been subject to severe court challenges, for although there are aspects that are outdated it is relatively straightforward and clear. It provides regulatory certainty that is valuable for investors and operators.

Dominance, a concept from competition law, does not provide this certainty and clarity. It is a post-hoc concept, used for specific cases, and we would be concerned that its adoption for EU regulatory purposes could be counterproductive. I may say that we have consulted with the Competition Authority in Ireland on this matter and the view is shared by both agencies.

The Commission has proposed a complex, two level mechanism, involving dominance for the heavier obligations of the regulatory framework. We argue very strongly for this to be revised and the simpler mechanism retained. Regulators work ex-ante and must have clear tools to be effective. There is a separate argument as to whether significant market power should kick in at 25% or at some other percentage, but I do not propose to go into this here. My key point is that the quality of the regulatory regime – as well as its implementation – can have very profound effects on how the market develops. These are not just theoretical models for debates among experts.

Future Developments

Having consulted widely, the commission is currently revising its proposals. The European Parliament will debate them in May and the Commission will then come back to the Council in June. There is great anxiety to move to conclusions rapidly as evidenced by the Lisbon summit. I share that impatience, while recognising the scale of the tasks.

Conclusions

When Commissioner David Byrne gave the first speech on regulation last January he said:

'The impact of globalisation and electronics have combined to transform the economic and social landscape beyond recognition. The economy is now becoming a hyphenated e-economy, whose borders are difficult to define, and whose motive forces are more difficult still to channel and police. Society, although not yet a virtual 'society.dot.com' is evolving into a radically diverse archipelago of interests, networks and competing values. Whether you are a policymaker at European or national level,.....in today's environment – you are confronted with a complex reality. And change is the only constant factor.'

The task facing European policy makers in shaping a new regulatory framework for the next 5 to 8 years is formidable: it must be far-seeing and flexible in an industry for which 6 months is the long term: it must be strong and clear enough to withstand challenges, as it is itself used to challenge the status quo to the benefit of the user. In Ireland, we have recognised the importance of telecommunications to our own future, and indeed our markets are principally in the EU. We must make the most of our opportunity to influence its shape, not just for narrow national interest however, but for the prosperity of the EU as a whole.

Thank you