

Effective Harmonisation within the European Electronic Communications Sector

A consultation by ERG

1. Introduction

The European Regulators Group (ERG) was established under the EU electronic communications regulatory framework of 2003 “to contribute to the development of the internal market and to the consistent application in all Member States of the regulatory framework for electronic communications networks and services.”

Since 2003, the question of whether the Framework is delivering the required degree of harmonisation has been raised periodically. But it has proven difficult to obtain clear consensus amongst regulators, the Commission, European Parliamentarians and other stakeholders on this question. On one analysis, the Framework already provides for a considerable degree of harmonisation, requiring as it does the alignment of legal processes for authorising networks and services coupled with detailed instructions for national regulators on when, how and where to regulate. Nonetheless, there is a widespread belief, particularly amongst certain stakeholders, that more harmonisation is required and should be delivered.

This discussion paper sets out an analysis of harmonisation, looking at costs and benefits of different approaches, and sets out initial criteria by which the ERG can systematically examine and address the need for greater harmonisation and the depth of harmonisation required in different circumstances. The criteria outlined in this paper have been developed from an analysis of the costs and benefits of harmonisation to determine when it is efficient to pursue regulatory harmonisation within the sector and when it is less appropriate to do so.

ERG proposes that harmonisation should be a central theme of its 2007 Work Programme. It currently expects to prioritise and design its various harmonisation projects on the basis of the analysis in this paper. It does not regard the analysis as definitive however and would therefore welcome comments on both the analysis and on the priorities that have been derived from it.

This paper does not consider harmonisation within the context of radio spectrum management, nor does it consider the optimal institutional framework through which regulatory harmonisation might be achieved within the EU.

2. A means to an end: Harmonisation of the internal market(s) for European electronic communications

The EU's regulatory framework for electronic communications services (ECS) and networks recognises the need to shift the sector towards a more efficient and dynamic market structure, within which effective competition will lead to gains to the overall economic welfare of Member States and to Europe as a whole. It is also recognised that electronic communications markets incorporate critical network infrastructure and services which, in turn, stimulate economic growth and global competitiveness. A thriving, efficient sector will also bring social and economic benefits to European citizens who, as users, are able to exercise a choice of access to a range of information society services.

The process of transition towards a dynamic and competitive market model has taken place over a number of years, underpinned by several waves of EU legislation, each increasingly ambitious in scope. The current EU regulatory framework (from hereon, 'the Framework'), agreed by Council and Parliament in 2002, builds on earlier legislation abolishing special and exclusive rights and guaranteeing open licensing systems and a move to general authorisations. The major innovations in the new Framework have been the adaptation of established methodologies used in competition law and the close alignment of national regulatory mechanisms with one another, in particular those governing the identification of 'Significant Market Power' (SMP) and the application of regulatory remedies designed to promote effective competition where such SMP exists. This has led to increasing responsibility being granted to the European Commission, as the ultimate supervisory body for the Framework as a whole, and specific responsibilities being placed on national regulators. These include not only everyday duties of application and enforcement of national regulatory provisions but supra-national responsibilities, operating within the Framework of the European Regulators' Group (ERG), to co-operate with one another and the Commission and to advise the Commission in the performance of its functions.

2.1. Defining harmonisation

"Harmonisation" is a word in everyday use amongst regulators and stakeholders with a particular interest in regulatory policy and practice, despite the fact that it is not a word which appears in the Directives. Nevertheless, Article 7(2) of the Framework Directive, can be taken to set out the fundamental NRA responsibilities concerning harmonisation:

"National regulatory authorities shall contribute to the development of the internal market by co-operating with each other and the Commission in a transparent manner to ensure the consistent application, in all Member States, of the provisions of this Directive and the Specific Directives. To this end, they shall, in particular, seek to agree on the types of instruments and remedies best suited to address particular types of situations in the market place".

This provides a general idea of what is meant by harmonisation but still leaves much open to debate. What is meant by “consistent” application? At what level should “consistency” be achieved? Consistency in the general approach, in the types of instruments and remedies applied or in the detail of those instruments and remedies? How exact should the required agreement on “the types of instruments and remedies best suited” be?

Should a preferred remedy (or set of remedies) be identified for each situation? Or should we expect that similar situations can often be dealt with equally effectively by different regulatory approaches? If the latter, are there nevertheless circumstances where the uniform solution is necessary and how can these circumstances be identified?

This paper addresses all of those questions and reaches some provisional conclusions.

2.2 ERG harmonisation work to date; scope for follow-up

ERG has already reached collective agreement on a number of issues, all relevant to this responsibility to promote consistent application of the Directives, for example:

- Revised ERG Common Position on the approach to appropriate remedies in the ECNS regulatory framework ("Remedies" document) ([ERG \(06\) 33](#));
- Public Mobile Termination Rates Benchmark - updated to January 2006 ([ERG \(06\) 24](#));
- Common position on EC Recommendation on Cost accounting and accounting separation [ERG \(05\) 29](#); and
- Common Statement on VoIP regulatory approaches ([ERG \(05\) 12](#))

However, the Commission and a number of industry stakeholders have commented that ERG guidance produced so far has been insufficiently detailed and/or prescriptive to achieve “consistency”. As a result, in their view, application of the Directives cannot yet be regarded as “consistent” across Europe. This paper attempts to answer two questions therefore:

- In which areas of regulation is there the strongest case for early action to improve “consistency”?
- In those priority areas, how detailed and prescriptive does ERG collective agreement need to be to achieve “consistency”? To express the same question using different words:

- how uniform do the national regulatory remedies need to be; or
- at what depth should remedies be harmonised?

2.3 Criteria for prioritisation of harmonisation work and for assessment of the depth of harmonisation needed

Annex A discusses the main theoretical arguments which have been put forward to illuminate discussion of the case for more or less harmonisation. Synthesising this work and applying it to electronic communications networks and services, we have drawn the following conclusions in terms of identifying the criteria for prioritisation of harmonisation work:

Services with Pan- European potential

A high degree of consistency is required in order to facilitate the emergence of “tetherless” services which can in principle be provided remotely to the customer from any physical location. In the absence of such consistency, the pan-European potential of such services cannot be realised. Voice over IP (VoIP) is a prominent current example where such potential is not currently being realised, as a result of differences in the general authorisation conditions across Europe, including access to emergency services, numbering policy, entitlement to number portability, and so on. These differences currently make it uneconomic for VoIP providers to offer a common service to customers across Europe.

The increasing use of reliance of networks on IP is likely to increase the range of services where such a high degree of consistency is necessary. However, for the moment, most ECS cannot be offered on a pan-European basis.

Services with a significant cross-border dimension

A high degree of consistency is also required for services with a significant cross-border dimension, even where it is not realistic to suppose that a single service provider could address a European customer base. Wholesale international roaming is the most prominent current example of such a service. Even though there is general agreement that wholesale prices are too high, no NRA has strong incentives to price-regulate unilaterally as the beneficiaries of such regulation are overseas network operators and (ultimately) consumers based abroad. Moreover, home consumers do not benefit at all and may actually be worse off if regulated networks raise domestic charges to recover wholesale roaming revenue lost. Consistent multilateral regulation overcomes this problem of mismatched incentives.

Other examples in this category may theoretically arise where inconsistent regulation across national boundaries gives rise to distortions in one national market or the other. Termination has sometimes been cited as an example of

this phenomenon although ERG is not aware of any evidence that such an effect is material.

Since roaming is being addressed by a bespoke regulation, there may be no cases in this category (except possibly for termination) which require prioritisation in ERG harmonisation work.

Promotion of efficient investment and market entry

Sufficient consistency is required to facilitate efficient investment and market entry by overseas players. Theoretically, entry could be deterred if differences in (otherwise effective) national regulatory regimes gave rise to significant costs which would be avoided by more consistent regulation. In practice, it is hard to find real examples of such a phenomenon. However, entry is undoubtedly deterred by lack of availability of inputs for the provision of particular electronic communications and online services which can be exacerbated by the ineffective regulation of dominant players. Entrants will find it hard to justify their investment costs if the competitive landscape is heavily tilted against them.

Consistency or uniformity?

It is important to maintain focus on consistency rather than uniformity although the two are often confused. A “one size fits all” approach to regulatory remedies is sub-optimal where national market differences demand different solutions in order to ensure a good deal for consumers right across Europe. Additionally, different remedies may be more or less equally effective at achieving a particular desired result in which case rational investors should be indifferent between them. Where this is so, it is (at best) pointless and disruptive and is potentially costly to change detailed rules purely so as to achieve uniformity. Further, the importance of new approaches should not be under-estimated. If all NRAs are constrained to adopt uniform solutions, it will be unlikely that good new approaches can be considered seriously.

Examples of a misguided uniform approach to regulation would be:

- A single European price for an unbundled local loop or for mobile termination. Cost differences between different provider networks very frequently mean that one or more of the regulatory objectives of Art 8, Framework Directive, could not be satisfied by a uniform pricing policy.
- A uniform requirement governing the forms of bitstream access available. The choices made will need to take careful account of network topology, customer density and a host of other essentially local parameters.

2.4 Preliminary views on harmonisation priorities

The above considerations provide a basis for ERG to form an initial view on the prioritisation of work on harmonisation and on the degree of uniformity of remedies implied by the need for sufficient consistency of approach to deliver the single market

a) Regulation of VoIP

There is a strong case for reviewing the [ERG Common Statement on VoIP](#), that was issued in February 2005 with the intention of achieving a much higher degree of consistency of ERG's approach to the regulation of the VoIP market than at present.

b) Regulation of key wholesale access services in markets where a position of SMP has been identified

It is clear that there no single market in any wholesale network access product (unbundled loops, bitstream access etc) is remotely in sight. These are products for access to national (or more local) networks. An unbundled loop needed in London is not substitutable by an unbundled loop available in Warsaw. Therefore, the harmonisation question relevant to these products is the degree to which uniformity of remedies is necessary to deliver a single market in downstream services. As discussed above, near-uniformity of remedies can undesirable and impractical in many such cases. Even where market circumstances are similar, it is not at all clear that near-uniformity of remedies is necessary to deliver the single market.

ERG believes that widespread dissemination of best practice in the choice of remedies will lead to an *appropriate* degree of harmonisation (or "consistent application"). This may lead to great similarity of remedies across national markets in some cases but not in others. Near-uniformity of remedies will be a result of application of best practice in certain cases, not an end in itself.

Whether or not near-uniformity of remedies is the result, the intention should be to achieve regulation which is uniformly effective, in the sense that it maximises the prospects for efficient market entry and competition in downstream markets while avoiding both distortions of investment decisions and exploitation of market power. All European consumers will thereby benefit from more vigorous competition, better services and greater choice in end-user markets.

Wholesale access products account for 11 of the 18 markets identified in the Commission's original 2003 Recommendation on relevant markets. For 2007, ERG proposes to give priority to:

- **Broadband access markets** (full and shared access to unbundled loops; bitstream access) as regulation is still at a relatively early stage in these markets which are of vital importance for a large range of services of huge significance in the business and residential market segments
- **Fixed and mobile termination markets** as significant methodological issues remain to be resolved concerning the timing of cost recovery, principles of allowance for major new investments and questions of efficient scale in these markets

c) Vital generic issues

There is a strong case for continuing to deepen our understanding and dissemination of best practice on generic issues which are vital to effective access regulation. These include:

- Costing methodologies
- Differentiation of access remedies, as between new and existing infrastructure
- Avoidance of margin squeeze

Again, an appropriate degree of harmonisation will follow from widespread dissemination of best practice

3. Conclusions

Taking forward its work on harmonisation, ERG proposes to concentrate of widespread and rapid dissemination of best practice, rather than striving to achieve uniformity of remedies as an end in itself. In general, it believes that this is the right route to fulfilment of the objective of consistent application of the Directives. And it will promote uniformly effective regulation across Europe so as to achieve the regulatory objectives set out in Article 8 of the Framework Directive.

However, there will be situations where special efforts need to be made to promote a greater degree of uniformity. This applies where the service under regulation has pan-European potential which will not be realised without a sufficiently close alignment of national regulatory approaches.

ERG welcomes comments from stakeholders on the analytical Framework set out in this paper and on the proposed priorities for harmonisation.

Consultation closes 15 January 2007

ANNEX – A SUMMARY OF THE MAIN THEORETICAL CONSIDERATIONS

The benefits of harmonisation

The above analysis suggests that even where there are market imperfections that might justify intervention, or where the costs of some providers can be reduced by regulatory harmonisation, it must be demonstrated that the economic benefits of harmonisation outweigh the economic costs.

The typical arguments in favour of harmonisation are:

- *The facilitation of cross-border trade.* At the most basic level, open trade promotes greater economic welfare by stimulating efficiency in supply and by allowing economies of scale to develop. However, electronic communications services (ECSs) provide an interesting counter-factual case in that the types of services which are typically heavily regulated (access and access-related products) can also only be ‘sold’ in a single geographic location. It is not possible, for instance, to sell local loop unbundling across borders.
- *Elimination of cross-border externalities.* This is the main reason for regulatory cooperation. If national rules have effects on other countries or externalities, coordinated decision-making and the adoption of common rules can, in principle, raise overall welfare through two effects: externalities are internalised and compliance with multiple rules is eliminated. This argument has been used in the past to justify co-ordination of standardisation decisions and mutual recognition of ‘Type Approval’ for electronic communications apparatus. The adoption of common rules addresses the problem of “regulatory fragmentation” which occurs when the decisions of distinct national authorities are incompatible or contradictory¹.
- *Reduction in the costs of regulatory compliance* for business when operating across multiple regulatory jurisdictions²
- *Harmonisation prevents investment distortions.* In particular, where a Member State’s laws and regulations are harmonised with those of its major trading partners this may encourage the location of multinational firms in that Member State and the retention within that Member State of firms that develop multinational operations³. In the case of ECS networks, it is argued that heterogeneous regulations may distort investment incentives or operating behaviour as carriers are encouraged to venue shop or otherwise arbitrage

¹ Nicolaides, page 3.

² Quigley, page 9.

³ This is an important concern because serious distortions may occur where governments act in favour of their “national champions”, thereby distorting competition conditions within the pan-European environment. Gual, page 13.

regulatory distortions.”⁴ On this analysis, it is not the scope for actual trade across borders that matters as much as the ability for companies to make investment decisions in ECS markets throughout Europe, unfettered by differences in regulatory approach⁵.

Limitations on scope for harmonisation

The above analysis makes a strong case for further harmonisation by NRAs and the Commission being pursued in an evidence-based, focused way which recognises that some areas should be prioritised for greater harmonisation of approach. On the other side of the equation, we believe that some forms of harmonisation applied in some market circumstances would be positively harmful.

The arguments against complete harmonisation can be summarised as follows:

- There is a need to take account of differences in local circumstances and to utilise detailed knowledge of local market that national regulators possess. This implies that in most cases, it will be appropriate for national regulators to have the scope to vary remedies at least to some degree.

An obvious example of this relates to the way that access remedies are designed to facilitate the most widespread infrastructure competition. The theoretical case for infrastructure competition being superior to services competition is strong. An ideal environment would be one which supported enough end-to-end access infrastructure providers to create self-sustaining infrastructure and services competition. But in practice, such a market outcome is highly unlikely to arise in many Member States because geographical factors and economies of density will not support more than one, or at most two infrastructure providers across much of the country. Striking the right balance between access infrastructure and unbundling regulation, and between wholesale unbundling and wholesale managed

⁴ Lehr & Kiesling, page 4.

⁵ It is worth noting that investment decisions will be primarily driven by the level of expected returns and the risk and uncertainty associated with those returns. Regulation will be one factor in determining risk and returns, but there will be other economy-wide factors, factors specific to the e-communications market, and company-specific factors which are also relevant. It is important not to assume that regulatory harmonisation can lead to an equal propensity to invest in all Member States. According to the recent London Economics/PWC study for the European Commission, other factors that have an important positive influence on firms' investment levels such as GDP per capita, the land area and population density of the country in which they operate, the size of the company, incumbent status and whether the firm operates in more than one sector. Indeed the study highlights the modelling of supply and demand of telecom infrastructure by Røller and Waverman (2001) find that GDP per capita has a positive and significant effect on the demand for investment. See London Economics, page xii.

services competition, relies on the national regulator taking careful account of these empirical factors as they apply in that Member State.

- Innovation and experimentation: in fast-moving and innovative environments, some diversity of regulatory approach can be positive, as it allows Member States to experiment or learn from each other, provided best practice is then filtered upwards through a network of regulators and even into European legislation over a period of time⁶.
- There may be instances where it is more efficient to agree a non-harmonised standard over a harmonised inefficient standard particularly in cases where it is clear that a 'one size fits all' approach to regulatory policy across countries is inappropriate.⁷
- Harmonisation may have costs for a member state if the optimal form of regulation depends on institutional features of the economy.⁸ Regulatory approaches that are suitable for more developed Member States cannot be applied to less developed countries without significant risk of setting standards or imposing industry structures that are inefficient in the context of that market: this would certainly be the case with some of the accession countries that are due to join in 2007 and 2010.
- Finally, as long as Member States have independent, national courts and regulators even the adoption of completely identical regulations will not guarantee that the same wording in a regulatory statement or the same regulatory structure will result in identical interpretations of decisions. This is important because it means that regulatory harmonisation cannot remove from investors many of the costs of understanding unique features of a market within a particular Member States that some operators argue is the case.⁹

It is worth noting that, out of the 136 operators that were surveyed by London Economics/PriceWaterhouse Coopers only 6 per cent of respondents indicated any further desire for greater harmonisation of the Framework¹⁰.

⁶ Nicolaidis, page 3.

⁷ Geiger (1998) in Quigley, page 9.

⁸ Quigley, page 6.

⁹ "According to Lloyd (1997) the feasibility of achieving harmonisation, defined depends on the balance between what he describes as 'quantitative' and 'qualitative' harmonisation. Specifically, where there is only one object to be harmonised, for example, tariff levels, harmonisation can be termed 'quantitative'. In contrast, where regulatory policies have multiple dimensions or elements, harmonisation will be qualitatively-based. Lloyd, argues therefore that harmonisation will almost always be partial and minimum standards are the most achievable and most likely form of harmonisation". In Quigley, page 2.

¹⁰ London Economics, page 112.

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