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## Broadband & Mobile Featured Article

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### Open Networks Not the Issue



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Software developers are in favor of "open networks and devices" for a really simple reason: it's the foundation of their business models. Mobile network access providers are more circumspect for equally simple reasons: it complicates their packaging challenges.

Most consumers probably do not yet have opinions about the matter. Most never will. What consumers will care about and respond to are the likely changes in the way they buy service and devices. These days, the overwhelming majority of customers buy subsidized phones on multi-year contracts. In an open networks environment they can pay retail prices for their devices and then buy service without a contract.

For most users, that is the big change, not the applications they might or might not want to use. Over time that might change. As people become more accustomed to the idea of "no-contract, pay full retail for your phone" packaging, more may opt to do so. Most will probably opt for cheaper phones.

"We've conditioned customers by putting very expensive computers in their hands for very few dollars," McAdams said to a CTIA: The Wireless Show audience. "It will be a big transition."

But there are other issues to weigh. Some policy advocates now argue no mobile providers should be allowed to offer bundled phones that are "locked" to a particular service provider. The argument is that the practice artificially restricts competition, since consumers are not free to take their phones to another provider.

But economists at the Phoenix Center say higher prices would be the inevitable result of such prohibitions on device locking and contracts.

"There is no free lunch," says George S. Ford, Chief Economist of the Phoenix Center and co-author of a new study about consumer welfare and prohibitions on phone bundling with wireless service.

"The typical consumer wants a free or very low cost cell phone, and mandatory wireless Carterfone rules would eliminate the incentive to offer such discounts," says Ford. "That will have consequences: all consumers will pay higher prices, while only the few more sophisticated users would likely receive any benefit from such regulations."

The Phoenix Center analysis also demonstrates that the steep discounts and subsidies on wireless handsets in fact require a strong compatibility between the equipment and the services. In other words, though unlocked devices offer benefits of one sort, tight integration offers benefits of another sort, not restricted to lower-price phones, but also extending to user experience.

The reason Apple appliances work so well is that Apple tightly controls software and hardware. Mobile providers not only argue this also is necessary for smarter mobile devices, but also the key to lower device prices.

Carterfone-style regulations explicitly lower the incentive for wireless providers to offer handset subsidies. As a result, should policymakers impose wireless Carterfone obligations, consumers would pay more for mobile handsets, the Phoenix Center economists argue.

It is an almost-classic case of good intentions leading to advocacy of policies that might make a problem worse, or lead to new problems. Many assert that mobile providers in the United States, "through term contracts, early termination fees, and allegedly restrictive handset certification and support policies, abuse their position in the market in order to lock customers into service contracts, limit consumer choice, and hinder mobile handset innovation," says Ford.

"The main implication of the analysis is that any prohibition on coupled and subsidized handsets is not certain to improve customer welfare as a matter of theory and will, in fact, quite plausibly reduce consumer surplus," the Phoenix Center says.

Sometimes we tend to focus on the undeniable advantages of open software platforms as the primary way consumers can benefit from openness. At least some observers think the disadvantages to consumers, in terms of higher device prices, must be considered as well. In a market where consumers freely can choose to own their devices and buy service without a contract, or take a subsidized device with a contract, most consumers probably will choose the cheaper phone option.

In a market where it is illegal to offer contracts or locked phones, higher phone prices are the inevitable result, as there is no incentive for the service provider to subsidize the phones. Good intentions do not always result in good policy.

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