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PERSPECTIVE:
WHY LOCAL ACCESS IS KEY TO “FREE” NET COMPETITION

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The “free” Internet movement is the hottest thing to hit Europe since sliced toast. Unfortunately, however, there really is no such thing as a “free” lunch.

“Free” Internet service is really a bundled product made up of two discrete inputs: the origination portion of the call – dominated by the incumbent – and the termination end of the call.

Regulators seem pleased with the impact of “free” Internet service on the structure of the market. For example, U.K. regulator Oftel noted that its current Number Translation Services formula has encouraged the development and growth of new services including those related to the Internet. Moreover, Oftel was not convinced that originating operators are being insufficiently rewarded for their network investments. To the contrary, the regulator found that incumbent operators are “recovering their costs . . . including those costs associated with additional investment and an element of profit through a return of capital.”

Yet, notwithstanding these statements, Oftel believes that its NTS formula should be revised.

Maybe it’s just me, but I simply don’t understand such regulatory schizophrenia.

On one hand, to the extent that there are legitimate problems with the existing NTS formula (e.g., geographic averaging), then Oftel should fix the problem immediately and move on.

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On the other hand, if Oftel does not act carefully, then it will make entry [or continued operation] in the “free” Internet market so expensive as to be unprofitable. When this occurs, consumers are worse off because they will have fewer services to choose from as well as less competition in prices.

So what can we do about all of this? Obviously, the immediate short-term solution is to ensure that any revisions to “free” Internet formulas fix legitimate problems and are not used by incumbents to deter or prohibit new entry.

But the inquiry does not end here. Clearly, the problem rests with incumbents’ control of the local access market. As such, long-term solutions are also required.

First, regulators must remove all residual barriers to facilities-based entry for alternative broadband networks and technologies. Without increasing competition on networks, regulators will realize fears of a “static, incumbent-centric perpetual resale” model. Concurrent with this first step, regulators must also implement promptly effective local loop unbundling and collocation rules. Such rules are needed immediately because only incumbents “with their dominant control of the local loop” are currently able to provide xDSL service. As such, as demand for high-speed broadband service grows, it seems highly unlikely that a “free” service that provides access only at 28 to 56 kilobits per second will provide much of a competitive threat to a incumbent-controlled vertically integrated service that provides Internet access at speeds from 1.5 megabits per second.

Regulators therefore should not accept incumbents’ arguments that they should eliminate competition in exchange for Faustian political promise of immediate broadband deployment. This is the inherent fallacy of the “choices” over “competition” argument. Instead, regulators should do everything in their power to stimulate additional demand, for as demand grows, so will the incentive for additional firms to invest in advanced broadband networks in Europe.