

---

# Smart Regulation and Competition Policy in Electric and Telecommunications Markets

Prepared for the Texas Public Policy Foundation  
8<sup>th</sup> Annual Policy Orientation for the Texas  
Legislature  
January 14, 2010

Jerry Ellig  
Senior Research Fellow  
[jellig@gmu.edu](mailto:jellig@gmu.edu)

---


MERCATUS CENTER  
GEORGE MASON UNIVERSITY


---


# What is the goal?

“If you don’t know where you’re going, any road will take you there.”

-- George Harrison

 **Consumer welfare:** Every unit of every resource employed in the use that produces the most value for consumers






 **Affordability:** Every consumer has the opportunity to purchase some minimum level of service regardless of income or location

 **Public safety:** Network must support certain services even if many consumers might not opt to purchase them

---

---







# Why consumer welfare?

-  Treats electricity and telecom the same way antitrust treats other industries
  -  Good for consumers
  -  Prices reflect costs; services offered when they pass cost/benefit test
  -  *Sustainable* innovation and job creation
  -  Forces companies to focus on satisfying consumers instead of wasting resources lobbying
-

---







# When consumer welfare isn't enough

*Accomplish other goals with least possible sacrifice of consumer welfare*

-  Identify specific, concrete outcome sought
  -  Measure it
  -  Identify alternative policies
  -  Assess how each alternative will affect amount of desired outcome
  -  Assess how each alternative will affect consumer welfare
  -  Decide how much consumer welfare is “worth” sacrificing to accomplish how much of the other goal
-

---

# Regulated monopoly paradigm

-  Entry controlled
  -  Prices regulated
    -  Price levels based on average costs
    -  Price structure promotes opaque cross-subsidies
  -  Service quality and other contract terms regulated
  -  Exit prohibited (provider of last resort)
-

---

# Competitive market

 Entry and exit relatively easy

 Prices and contract terms set by competition

 Policy focuses on monitoring and preserving competition





 Consumer protection regulation focuses on providing information and preventing fraud

 Subsidies are transparent and funded through efficient mechanisms

---

---

# Texas electricity

-  Customers within the Electric Reliability Council of Texas (70-75% of state) can choose retail electric providers
  -  99.7 percent of these customers have more than 5 retail electricity providers available
  -  Transmission/distribution remain regulated
  -  Retail competition delayed indefinitely elsewhere
-

---

# Texas telecom

 85% of cities have 3 or more telecom providers


 79% of Texans have wireless phones

 86% of counties have 2 or more broadband providers

---

---

# Smart regulation

 Grant a monopoly only when natural monopoly is proven to exist

 Price regulation incentivizes innovation

- Deliberate: Price caps
- Unintentional: Regulatory lag





 Subsidies are transparent and funded through efficient mechanisms

 “Provider of last resort” can use low-cost technology (eg satellite phone)

---

---

# Understanding unseen consumer costs

-  Higher prices = fewer consumers subscribe or use the service
  -  These consumers lose difference between what the service is worth to them and what they would have paid for it
  -  Firms lose operating profit on these consumers
  -  Loss is big when demand is sensitive to price (eg, wireless, video, broadband, long-distance phone)
-


---

## Example: Effects of Texas USF settlement

 High-cost subsidies cut by \$144 million (36.5%) by 2012

 Assessment fell from 4.4% in 2008 to 3.4% in 2009






 Phone companies can seek higher monthly rates

 Increased usage due to lower prices on price-sensitive services will benefit Texas consumers, phone companies, and taxing authorities by \$43.5 million annually *even if* basic local phone rates rise

---

---

# Competition policy

-  Ensure that licensing/registration requirements are no greater than necessary to accomplish policy goals
  -  Price for “basic” or “POLR” services should not undermine competition
  -  Competition should determine service quality and other contract terms
  -  Consumer protection should encourage information disclosure and prevent fraud
  -  Subsidies are transparent and funded through efficient mechanisms
-

---

For more information ...

Search for Mercatus Center studies on  
telecommunications, broadband, cable, and  
electricity at

[www.mercatus.org](http://www.mercatus.org)

Read daily commentary on technology policy at

[www.surprisinglyfree.com](http://www.surprisinglyfree.com)

---