

## **The Public Choice View at the “Deregulation” Movement: Analyzing the Experience of European Telecommunications**

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### Abstract

**Purpose** – The liberalization of European telecommunications has been expressed in highly concentrated markets with several major players at the pan-European level. Instead of fostering competitive marketplaces, the reform has created an oligopolistic landscape with powerful private corporations. This induces reasonable questions about the real objectives and the chosen ways of the reform.

**Methodology/approach/design** – The deregulatory movement in the telecommunications sector is analyzed through contrasting perspectives of the public interest approach and public choice theory.

**Findings** – The chance to change the landscape of the industry has been missed, and the current trend towards the global oligopolistic marketplace yields an unprecedented amount of economic power to narrow groups at the global scale. The liberalization movement introduced market mechanisms in the industry, but the real free and open market has never been formed, and it is possible to assert that it has never been among the real objectives and intentions of the policymakers.

**Originality/value** – The recent surge of “liberalization” in the telecommunications industry speaks rather in favor of the hypothesis of vested private interests in the policy and that they have always been greatly covered by the sauce of public interest justifications. The case of telecommunications shows that ideas and understanding of economic phenomena played an important role in adoption of regulatory regimes, and it is apparent that people on the top of the social pyramid have opportunities to pick up and foster those ideas that better fit their private needs.

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## 1. Introduction

The nature of state interventions into economy might have different explanations, and two opposite extremes are public and private interests (Buchanan and Tullock 1962; Laffont and Tirole 1991). When the interventions are justified by the public interest, the classical arguments stem from the market failure explanation, and sometimes take a form of appeals for social justice, humanism, safety and security and other concerns that are not directly connected to the efficiency problem, but that are supported by theories and concepts from political philosophy and social sciences (see, e.g. Stiglitz 1988). Public choice theory, developed in the 1960s, has promoted the opposite view at public policy and underlined that the main driving force of political decision-making processes is private interests of individuals (Peltzman 1989; Buchanan and Tullock 1962; Tullock, Seldon and Brady 2002).

Since the time of appearance of this public and private interest separation in the economics mainstream, many scholars have tried to analyze various economic problems from these contrasting perspectives (e.g., Laffont and Tirole 1991; Djankov et al. 2001). The present paper is an attempt to contribute to this scholarship and to apply these opposite views to the deregulatory movement in the telecommunications sector with a particular focus at the European experience. The results of the liberalization reform in the industry are highly concentrated markets with several major players at the pan-European level, and this induces reasonable questions about which kind of interests, public or private, have prevailed in the chosen way of liberalization.

The article begins with a brief review of public and private interest theories of regulation. After that, it examines the applicability of these theories to the liberalization reform of the telecommunications industry. The main argumentation of the paper is concentrated around the position that although the objectives of the reform indeed represented the public interest view, there are several questions that are better described by the public choice approach. The paper examines alternatives that could be adopted by the regulators, arguing that these alternatives also fit the concept of public interest, and analyzes why this choice has not been made.

## 2. Theoretical framework: The public interest concept and the public choice view

The idea of the public interest has been perfectly presented by Abraham Lincoln’s vision of “government of the people, by the people, for the people” and since the seminal work of Arthur Cecil Pigou, “Economics of Welfare”, has been embraced by the mainstream of economics as a response to the issue of market failures. The understanding that the market does not provide perfect solutions for a number of economic problems and that such imperfectness requires corrective interventions in the market performance has allowed to consider the government as a benevolent maximizer of social welfare (Laffont and Tirole 1991).

In addition to the market failure as a reason to intervene, there are also public interest theories that take into account non-“welfare maximization” objectives, such as public interest redistribution of resources to the poor or the disadvantaged, reduction of social subordination, obligations owed to future generations, protection of animals and wild nature, etc. (see, e.g., Sunstein 1993). Regardless of a theory that uses the public interest claim, and even in those cases when the concept is assumed as something granted for the analysis, it is crucial to keep in mind that the idea of the public interest is one of the most questionable, fragile and vague concepts that overwhelm economic theory (Buchanan and Tullock 1962). There are no tools that would allow to measure this phenomenon or that would provide robust explanation what the public interest stands for. There is no agreement, and, possibly, there cannot be agreement, about what is good and what is bad for our society, and, even if this desirability could be established, what are the best methods to achieve the desired outcomes (see, e.g., Hayek 1976). The concept has been vigorously criticized by many prominent pundits, economists and philosophers, because many of them have seen the public interest as simply “a rhetorical device that people use to persuade other people that they should agree to some policy they themselves favor.”<sup>1</sup>

Despite of this criticism, the public interest concept is a necessary tool for justification of political decisions and government actions, and cannot be avoided by society. Even the assertion of scholars, such as Hayek, that social justice is a meaningless term, that the role of the state is not to provide remedies for market failures and not to establish any goals for social and economic activity such as welfare maximization or efficiency, but to establish rules of just conduct and to allow “spontaneous order” to put everything on the proper places (Hayek 1976),

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<sup>1</sup> See, e.g., an analysis of views of Karl Popper and Friedrich Hayek on the public interest in Notturmo (2015).

in order to be accepted requires vigorous justification that might be provided only through the position of the public interest.

In any case, the public interest assumes a choice between different alternatives, and even if we suppose that in some ideal situations the policymaking process is not affected by rent-seeking behavior, lobbying, bribery or other forms of corruption, i.e. the process might be analyzed through the lens of public interest theory, the policymakers still cannot be free from their own beliefs, epistemological limitations and their own understanding of which alternative is better suited for social needs. As a result, the public interest might be considered as an outcome of a system based on the spontaneous order idea, i.e. a system that does not envisage achievement of any aims at all and, thus, does not incorporate not only private interests, but that is also not affected by any subjective views and biases.

The ambiguity and vagueness of the public interest perception is not the only weakness of the concept. The explanatory power of the concept is mainly focused around reasons and objectives of regulation, while the chosen ways of the achievement of the goals very often remain without convincing answers. The concept is unable to explain why the particular aims or methods of their achievement have been adopted when alternatives could also be sufficiently supported by the public interest argumentation, and this gap has been filled up by public choice theory.

The alternative to the public interest view on regulation is an understanding that in the real world, in contrast to the idealistic models, all economic actors have their own personal interests and make their decisions with these private objectives in mind. Public choice theory, being one of those endeavors in modern economics promoting an alternative to the public interest view on the political decision making process, claims that the government rather than to be “of, by and for the people”, is merely an instrument in the hands of some people (Tullock, Seldon and Brady 2002). Buchanan and Tullock (1962), who are among the founders of public choice theory, comparing the pursuit of the public interest with searching for the holy grail, reject the usage of the concept apart from “the separate interests of the individual participants” as meaningful and suggest that the public interest is never defined.

Croley (1998), describing the public choice theory of regulation, points out that this approach analogizes regulatory decision making to market decision making in a particular market where actors exchange “regulatory goods”, such as subsidies, entry barriers, price regulation, etc. The demand side of this market is fueled by private economic interests of citizens and entrepreneurs, while on the supply side private economic interests of politicians are augmented by their private political interests. Taking into account that organized groups and powerful

business entities have significantly higher lobbying opportunities and incentives to influence regulation than individual voters, public choice emphasizes that “the regulatory market works ... to the advantage of organized groups with narrow interests,” rather than to society as a whole (Croley 1998, p. 39).

Generally speaking, public choice is not an alternative to the public interest concept, especially if we take the point of view such as of Richard Posner that the public interest doctrine is not an economic theory at all.<sup>2</sup> The public choice approach does not exclude the idea that the government might act in the interests of society, but underlines that the government consists of individuals that have their own personal interests. These personal interests of politicians and bureaucrats for some reasons and in some circumstances, may coincide with common public needs, and even when they are different, democracy provides some tools to affect the decision-making process. However, being no more efficient than free market mechanisms, democracy does not provide sufficient protection from incorporation of private interests in regulation and is even often used for their achievement.

As well as the public interest approach, public choice is not without drawbacks. Being one of the economic theories, public choice mainly perceives private interests in economic terms and faces difficulties in analyzing cases when actors have altruistic, unselfish or public-spirited behavior. However, the major problem of private interest theories is that we hardly know anything about real interests of analyzed actors, about their psychological features and moral principles and, what is possibly even more important, about their actual relationships with other actors of the markets of “regulatory goods”. The result of it is that even when we have all reasons to argue that some particular decision has been affected by certain private interests, it still might be a case where the policymakers had other objectives in their minds or that this is a case of other private interests interactions than we assume in the analysis. Researchers that look at regulation from private interest positions might easily face counterarguments that they attribute hidden motivations to policymakers without sufficient evidence. At the same time, those who take the public interestedness as the foundation of political decisions for granted do not need to provide any support for their starting point.

In contrast to the public interest view, the power of public choice to serve as a guide in public policy is severely limited, and mainly might be expressed in appeals to deregulation due to the general pessimistic views of private interest theories about possibilities to promote collective welfare through interventions into market mechanisms. However, it should be noticed again that adoption of

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<sup>2</sup> Posner (1980, p. 503) notices that “public-interest theory is a description, rather than an economic theory.”

such policy as well as a choice of the ways of deregulation cannot be done without public interest argumentation, which inevitably leads to incorporation of private interests in the deregulatory move and that requires the tools of public choice in order to find out why the particular choice has been made.

Since telecommunications have always been a “laboratory” for regulatory experiments (Levi-Faur 1998), it becomes very interesting to look at the collision of public and private interest theories of regulation in their attempts to explain the biggest experiment that occurred in the telecommunications sector during the last decades of the 20s century and that still continue to affect the performance of the industry.

### **3. Public interest explanation of liberalization of the telecommunications sector**

It might be argued that the public interest approach gives a strong explanatory basis for liberalization of the telecommunications industry, especially if we look at the results. Modern telecommunications provide us a big variety of different services, many of which could even not have been imagined and could not be placed into policy documents 20-30 years ago. The introduction of market mechanisms, the appearance of private initiatives and technological progress have changed our world, making the industry one of the main drivers for economic development. Any arguments that preservation of the state-owned monopolies and state governance of the technological development could better fit the growing needs of our society would hardly be positively met by the contemporary scientific community.

Despite the vagueness and indefiniteness of the public interest concept, the liberalization and deregulation of the telecommunications markets is one of those cases where even critics of the approach might agree that it was a movement towards social needs. Some even argued that “social developments seemed to refute” the theories that look at regulation from the positions of private interests (Den Hertog 2010, p. 36). However, it seems that the public interest view does not provide a comprehensive explanation for at least for two aspects of the reform. The first is the timing, or more precisely why the process had not been initiated earlier, and the particular peculiarity of the issue is that the reform was enacted in a large number of world countries around the same period. The second is the way of the reform, or why the outcome of the reform was programmed as a set of oligopolistic markets that sometimes are represented in transnational oligopolistic form. Moreover, it is reasonable to find whether there were alternative ways for the reformation of the industry.

Many researchers connect the beginning of the reform with technological change that forced states to open their telecommunications markets (see, e.g., Stiglitz 1999; Laffont and Tirole 2000), and from this point of view policymakers had no choice, but to deregulate. Public interest theory explains it in the way that new technological solutions allowed to remove market failures that warranted the interventions in the preceding periods or that deregulation in the new technological environment is the more efficient solution for the market failure problem than regulation (Den Hertog 2010).

The first question that arises from this explanation is what was the market failure that supported the monopolistic nature of the industry? Despite the fact that the idea about natural monopoly characteristics of telephone services has been incorporated in the mainstream understanding of economics of telecommunications (see, e.g., Posner 1968; Joskow 2007), many empirical studies questioned this paradigm (see e.g. Evans and Heckman, 1983; Shin and Ying, 1992; see also the discussion in Spulber and Yoo, 2013). There was a large number of explicit claims about the artificial nature of such monopolies and the role of the government in their formation (e.g. DiLorenzo 1996; Thierer 1994; Trubnikov 2017b), and the example of the US industry in the early stages of its development shows that the industry could have a competitive form (Mueller 2013; Janson and Yoo 2013).

Moreover, the first years of liberalization in many instances were not the years that brought to the markets new services or advanced technologies. Of course, some subscribers benefited from new technological solutions in long-distance or mobile services, but for many the beginning of the liberalization just yielded ordinary phones in their homes.<sup>3</sup> While the state explained state control of the industry by the necessity of provision of socially valuable services for all members of society, these services, for a long time were rather luxury goods for a significant part of the households in many places of the world. The market had solved this public interest issue more efficiently and faster than the state during the previous years of inefficient state governance (see, e.g., Stiglitz 1999). Therefore, there are sound reasons to question the public interestedness of the government control of the industry before the liberalization period.

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<sup>3</sup> E.g., Armstrong & Sappington (2006), analyzing the development of the industry in Chile, show that “liberalization” allowed to increase the number of fixed lines more than three times between 1992 and 2000. Stiglitz (1999) notices that in many countries the reforms had expressed in “increases in the scope of telephone coverage and reduction of prices” (Stiglitz 1999, p. 5) and that “in many developing countries, entrepreneurs have ... demonstrated their ability to bring telephone services to poor villages” (Stiglitz 1999, p. 13).

The second question is what could be an effect of liberalization on technological development of the industry if the market mechanisms were introduced earlier, and we can assume that in this case we could face more rapid technological progress. As an example, digital switches and fiber optic, as well as, cellular telephony are the technologies that started spreading in the monopolistic industry in the 1970s-1980s and resulted in the growing number of networks subscribers, but they were not the technologies that were developed in the 1970s-1980s. Tim Wu (2010), for instance, argues that by 1916 AT&T already had "a working prototype" of a "wireless telephone", but since the technology was in the hands of the monopoly of the "wired" industry, it could not have chances to be driven by market forces.

The 1990s and 2000s were the periods where the market demonstrated how fast it is able to adopt and facilitate diffusion of technological advancements, reducing the costs of technological solutions and bringing the services into new areas, and, therefore, it is reasonable to suggest that the market could do it much earlier if the government did not suppress the market mechanisms in the industry. Of course, it might be argued that the level of semiconductor industry of that time imposed some limitations and that, for example, the weight of the first cellular phones made them inconvenient for subscribers or that the production cost did not allow widespread diffusion of the technology, but, at the same time, we have to admit that the state preservation of the monopoly until the last decades of the 20s century by no means played in favor of the industry development, cost reduction, and it is not clear whether it played for the public welfare.<sup>4</sup>

The public interest paradigm in the chosen way of the liberalization also induces a number of questions. Why had the industry not been torn apart in a number of independent enterprises, vertically and horizontally,<sup>5</sup> which could have helped eliminating the problem of market power and, thus, the necessity to create artificial competition? Why did the chosen way of the reform so vigorously require the slowness and prohibitiveness during the first phases of the process? Why might deregulation in many places of the world, in fact, be better described as re-regulation?

Answers of the public interest approach to the questions above might be based on prevailing views in economics of telecommunications, which payed significant attention to the natural monopoly characteristics of crucial parts of the

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<sup>4</sup> According to some estimates, the delay in introduction of mobile services in the US decreased consumers' welfare on dozens of billions of dollars (Hausman 1997).

<sup>5</sup> It is necessary to acknowledge that the pattern was not totally the same everywhere, but, nevertheless, the results of the liberalization are regulatory formed oligopolistic markets.



industry and high level of sunk costs of telecommunications networks. There were also concerns that liberalization could result in rates, as well as costs increases, reduction of service quality and R&D expenditures, problems with technical compatibilities and so forth. However, it is important to note that there was a lack of unanimity among the telecommunications policy scholars. Eli Noam (1993), for example, distinguished four main positions based on different combinations of antitrust and deregulation dimensions: anti-monopoly/deregulatory, anti-monopoly/pro-regulatory, pro-monopoly/deregulatory, pro-monopoly/pro-regulatory.

Some of the scholars from the anti-monopoly camp advocated the idea that “competition is needed to be established by intervention” and appealed to the divestiture of incumbents (see, e.g., Noam 1993; Burton 1997; Stiglitz 1999), but, nevertheless, even these anti-monopoly appeals have been severely limited by the mainstream theories. As a result, nowhere in the world a telecommunications marketplace dominated by small independent enterprises was formed by the “anti-monopoly” movement. There were examples of the USA, Japan, Russia, where the break-up of the former monopolies vividly played in interests of the public, but the policymakers did not envisage that the basic unit for the newly formed landscape could be a network within the coverage of a telephone exchange or a network of a scale of a city.

Despite the appearance of new technologies and advancements in economic studies, the natural monopoly belief did not vanish from the general understanding of the economy of telecommunications in the 1970s - 1980s. Nevertheless, the idea that not all parts of the industry share these natural monopoly characteristics eventually appeared in the mainstream. However, this did not challenge the monopolistic status of the local phone networks that was the core part of the industry providing customers access to not only local services, but also to intercity and international connections, and that eventually became a fundament for the construction of the broadband networks.

Many scholars and authorities in the 1980s claimed that “local telephone services seem to be generally accepted as a natural monopoly” (Breyer 1982, p. 291) and that without the natural monopoly argument “restriction of entry into the local telecommunications loop is not justified” (Spulber 1995, p. 34). Indeed, this justification could be the only plausible explanation of public interestedness in the preservation of monopolies in local parts of the telephone industry during the initial phases of the reform and slowness of the liberalization process.

The natural monopoly paradigm of the 20th century has not escaped from the policy even in the new era and continued to play an essential role as an idea of bottlenecks. Laffont and Tirole explicitly link the concepts of natural monopoly and bottlenecks in their highly-cited book “Competition in telecommunication”

(2000) when they argue that some segments of the industry are natural monopolies and that “these segments become bottlenecks”. They also point out that the location of the bottlenecks depends on the technology and that it changes with the industry’s evolution. Such a statement, as well as the attention that has been paid in the telecommunications policy to the problem of bottlenecks are vivid evidence that the natural monopoly paradigm, in fact, has never escaped the mainstream view on the industry, even despite the concept nowadays has been severely reduced to some particular segments of the field.

Meanwhile, from the history of competition in the early days in the US it is clear that the average cost curve did not have a downward slope (Mueller 2013), i.e. the industry was not an example of a natural monopoly according to the classical definition of the term. There might be a hypothesis that later technological development changed this feature, but this is not more than a hypothesis that has been questioned by many scholars (see e.g. Evans and Heckman 1983; Shin and Ying 1992), and even in the mainstream theory we could find statements such as “as more subscribers are connected to a telephone network, the average cost per subscriber may rise” (Joskow 2007, p. 1239). In other words, there is no robust evidence that theoretical models based on the natural monopoly concept have ever reflected reality, while they have always perfectly supported industry policy and continue to provide this support.

The understanding of telecommunications as an example of natural monopoly in one form or another ruled the reforms of the last decades in the majority of the world countries. The European “deregulation”, “demonopolization” and “privatization” reform of the telecommunications sector started in 1987 with the introduction of the "Green Paper on the Development of the Common Market for Telecommunications Services and Equipment" by Commission of the European Communities. The reform that put telecommunications services in the “market environment” took more than 10 years and did not allow competition in different fields of the industry at once (see, e.g., Larouche 2000).

Of course, if a company has invested in the infrastructure construction, a bigger number of connected users through this infrastructure will reduce the average cost. However, this, firstly, does not mean that if the industry consists of a number of companies operating in different districts, cities or regions, then this industry has higher average costs than it could have if the only one operator provides the services in the entire territory; and, secondly, it even does not mean that service providers operating in nearby areas and even in the same areas will not be able to benefit from economies of scale of their own networks, do their business more efficiently than a monopolist, and, at the same time, provide their

users the possibility to benefit from the total network effect through interconnections of their networks.

It might be argued that in such a case we face local monopolies, but if their operating area is sufficiently small, that means that overlapping of the areas is feasible and that the local monopolies are under pressure of potential entrance of the nearby competitors. It is very important to note that one of the mainstream theories — the theory of contestable markets — looks at the issues from the similar viewpoint. According to this theory, even those markets that have a monopolistic or oligopolistic structure might provide the same outcome as “perfectly competitive markets” if they are perfectly contestable (Baumol, Panzar and Willig 1982). Spulber and Yoo (2013, p. 5), for example, even argue that “[t]echnological change ... has made telecommunications markets contestable by reducing the sunk costs associated with market entry.” The deregulation movement had a chance to promote this kind of contestability in the industry. Deviation of such a monopoly from the optimal performance or opportunities for monopolistic competition due to technological pluralism makes overlapping inevitable if the network structure is represented by a number of independent networks, and, thus, these local monopolies could be easily destroyed by the real market process.

Moreover, the European reform could adopt the ordoliberal views at the competitive order, especially if to take into account the prevailing “mythology” about the ordoliberal nature of EU competition policy (Akman and Kassim 2010), but by that time the ordoliberal principles had been already replaced by the neoliberal outlook of the Chicago school of economics and “efficiency-enhancing rationale” (Bartalevich, 2016). While the ordoliberal school appealed for “creating an economy where production is decentralised and takes place in relatively small units” (Schnyder and Siems 2013), the mainstream ideology did not envisage such a competitive order for the telecommunications sector (Trubnikov and Trubnikova 2018).

#### 4. The view on liberalization through the lens of private interests

The economic theory of regulation describes deregulation from positions of private interests (see, e.g., Peltzman 1989). It is possible to distinguish different explanations of why captured regulation makes a choice of deregulation, especially taking into account that deregulation usually takes a form of a new regulatory environment, and among them the changing balance of political power of pressure groups or a decision of influential groups that they can better achieve their interests in an alternative regulatory regime (Peltzman 1989).

However, it possibly would be an exaggeration to claim that all regulatory bodies everywhere in the world were taken by the main interest groups and acted explicitly in order to put their private interests in the policy agenda. We also cannot neglect the role of international institutions and other forces that affected the liberalization movement in telecommunications. In such reasoning, Brady, for example, emphasizes the role of supranational institutions in the process such as the European Union, the World Trade Organization and the International Telecommunication Union, as well as positive experience of other countries (in Tullock, Seldon, and Brady 2002). Schneider (2001, p. 76), on the other side, analyzing the deregulation in Germany, France and Italy, points out the role of OECD and GATT, that have been used as “bargaining arenas” for the “US strategy ... to open international markets in this sector.” Levi-Faur (2005, p. 25), describing the rise of regulatory capitalism starting in the 1980s, points out the version that “international institutions, acting at least partially as agents of the United States,” have been the main sources of liberalization reforms in other world countries. Joseph Stiglitz (1998, p. 19), analyzing “the private uses of public interests,” notices that “international issues are probably more subject to capture.” In other words, it has become common in the academic society to suspect that international institutions serve the particular private interests of the most influential global groups, even if their positions have been supported by the claims about the national interests, and their role in the reforms of telecommunications policy is not an exception from this pattern.

Milton Mueller (2010) in his well-known book “Networks and States: The Global Politics of Internet Governance” points out that the world-wide liberalization of telecommunications was pushed by the US in the interests of the US economy. The traces of the US interests in the international arena have been augmented by business interests of leading players of the European advanced economies. Schneider (2001), for example, points out that European Commission’s allies and supporters in the mid-1980s were large European industrial firms such as Alcatel, Olivetti, Philips, and Siemens, and this statement in combination with the activity of AT&T in the European market at that time might explain why the first step in the liberalization was the opening of the market of telecommunications equipment (Trubnikov 2017b). There are also claims that for major European telecommunications enterprises, the opening of the international telecommunications sphere signified opportunities to expand their business empires and that these benefits outweighed the losses from the necessity of reciprocal duties to allow competitors to enter their local marketplaces (see, e.g., Clifton, Díaz-Fuentes, and Revuelta 2010).

Such views provide some alternatives to the public interest explanation of the liberalization of telecommunications at the end of the 20th century and give

answers to the questions about the timing and chosen methods. When we are looking at the field from the position of public choice theory, we have to bear in mind that the units of analysis are not companies or organizations, but individuals. The individuals might cooperate and form different groups with those who have similar interests or might be useful for a while, but, nevertheless, these private interests are the interests of particular persons. Moreover, these interests are not always expressed in financial terms, and often take a form of behavior that by no means can be considered as wrongdoing. If politicians even with a “good spirit” were keen to adopt particular methods of deregulation of the industry, they had to make a choice, and this choice had been affected by other people, who not necessarily were so public-spirited, and by experience of other territories, that had not necessarily been formed by uncorrupted policymakers. An alternative way to the reform could bring unforeseen results and it imposed risks on the decision-making process.

Liberalization went hand in hand with privatization, and it opened opportunities for some individuals to become owners of valuable assets, and sometimes the price paid for this newly formed property was lower than the real price or could be considered in this way. Acemoglu and Robinson (2012) in this sense point out the remarkable case of Mexican telecommunications industry, but even European countries where governments are often considered as more public-spirited, have also faced the situation when “today it is clear that the price could have been higher” (Florio 2007, p. 3). However, we can only guess why the price was in fact lower than it could have been, and private and public interest theories of regulation provide us totally different explanations. For those people who benefited from privatization, the alternative ways of telecommunications reform would not bring such benefits, but again they were not the only stakeholders of the industry. There were officials, bureaucrats and managers that governed the industry during the days of state-owned monopolies, and while the alternative would signify an immediate solution for separation of operational and regulatory functions,<sup>6</sup> for these stakeholders it could mean uncertainty of their future positions and personal incomes.

Another important issue of the “liberalization — privatization” reform is an attempt of governments to raise the revenues that they could receive from privatization, and here there is a clear contradiction between the goals of creation of a competitive market and maximization of the governments’ incomes. Business endeavors that promise monopoly profits cost higher than enterprises whose future positions are highly uncertain due to a competitive environment of the marketplace. From this point of view, preservation of significant market power of

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<sup>6</sup> It was clear that this separation was essential for the success of the reform (see, e.g., Melody 1999).

an incumbent allows to get higher revenue from its sale than if the company had been split up into a number of independent enterprises competing between each other. In many jurisdictions, privatization in the industry even assumed an “exclusivity period” for the incumbents, that, definitely, in the same way as the widely implemented delay in the placement of all services in the competitive environment, could not play in favor of competition (see, e.g., Wallsten 2004). As a result, privatization of telecommunications assets “in many countries failed to foster competitive markets, instead creating large private monopolies” (Wallsten 2002, p. 4).

Even the positive experience of the US divestiture of the former monopoly into 7 independent companies and the separation of local and long-distance business, was not considered as a guidance for others. On the contrary, there are totally opposing examples. For instance, the former Italian monopoly, that before the liberalization was represented by several companies, merged this assets in Telecom Italia in 1994 (see, e.g., GSMA 2013).<sup>7</sup> Some scholars, noticing that the “[a]greement between the political system and private interests in the field of telecommunications has been an integral part of Italian economic history,” openly name the Italian telecom privatization as an example of “privatization failure” (Florio 2007, p. 2). Another possibility for competition were cellular services that de facto represent a substitute for fixed telephony, but in a number of countries around the world, incumbents became major players in the new mobile markets, which again contradicts the objectives of formation of a competitive marketplace.

The slow pace of deregulation augmented by prohibition of competition in many markets in the initial phase, and allocation of radio resources for the incumbents, provided them opportunity to adopt their business to the changing institutional and, what was even more important for them, technological environment. The Internet was accompanied by a number of technologies that threatened the established order of telecommunications from different directions. New opportunities to use radio waves were opened, legacy copper lines were losing their value in the face of advancements of fiberoptic technology, the growing semiconductor industry was able to make totally obsolete the legacy communications equipment operated at that moment. Newcomers, once the industry was opened, could leverage implementation of new technologies and destroy positions of the incumbents.<sup>8</sup>

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<sup>7</sup> The consolidation decision was also adopted, for example, in Portugal, where previously the industry had a fragmented structure (see, e.g., Jordana, Levi-Faur and Puig 2006).

<sup>8</sup> See, e.g, the analysis of the regulatory impact on disruptive innovations in the wireless industry in Trubnikov (2017a).

The “public interest” in the European reform assumed formation of the “Common Market”, or what later has been transformed to the “Single Digital Market”, and that, basically, signifies the same players in all regions of the EU. Taking into account the incorporated belief about natural monopoly characteristics of telecommunications and the claims that the single European market will allow to benefit from economies of scale, that, according to some commentators of the reform, was not possible within the borders of one country (see, e.g., Koenig, Bartosch and Braun 2002), it is easy to conclude that the real purpose was to form the pan-European oligopoly with few beneficiaries among the most powerful actors of the industry. Only deregulation and liberalization were able to open international markets and allow the most influential global players to extend their operations in the new territories (Clifton, Díaz-Fuentes, and Revuelta 2010). Paradoxically, the development of the networks infrastructure in the west of Europe, at the same time, has been lagging behind many eastern European territories (see, e.g., FTTH Council Europe 2016), which according to the concept of economies of scale could not benefit from this phenomenon so much.

It is very important to underline that the period of formation of an industry is the most precious time for the rivalry fostering. This is the period of uncertainty, of entrepreneurial risks, of trials and errors that characterize the market process. This is also the period of empty fields and unsatisfied demand that open opportunities and create incentives for newcomers and discipline the leaders if they feel threats for their positions. In modern telecommunications, this period occurred in the 1990s-2000s and in many territories around the world, including European countries, the chance to create a real competitive market that could play for broad public interests and that could function without government support and regulation was missed due to the chosen policy of liberalization and deregulation. This choice has eventually resulted in the highly-concentrated area where the former monopolists have preserved their positions and their control over industry development, and where the most powerful of them have extended their business empires into new territories, forming the global oligopolistic marketplace.

The alternative to the formation of such an oligopolistic field was de-concentration of the industry, elimination of any economic power in the field, promotion of real rivalry between a large number of market participants and total exclusion of the government from the market performance. Laffont and Tirole (2000, p. 8) noticed that “many experts argue that regulation should end once local competition has developed and that regulation should be replaced by standard competition policy,” but the easiest way of formation of local competition was break-up of local monopolies. If competition was a target of the reform, then what could be a reason from the public interest perspective to wait for this development

of rivalry, when the competitive marketplace could be formed at once? The period when these monopolies were in the hands of the states was the best time for the formation of the competitive order, when de-concentration could have happened without raising the question about government intervention in market mechanisms and collision with arguments about private property. In this connection, Stiglitz (1999, p. 15), for example, noticed that “wherever possible [privatization in telecommunications] should preceded by the introduction of great competition, possibly through the extension of licenses to new private companies or by splitting up the telecommunications company.”

The answer to the question is pretty obvious from the public choice view. The real competitive order could never have been among the purposes of the policymakers, just because the groups and individuals that could benefit from the order are not organized and, thus, could not affect the policy. The power of the national telecommunications giants and those groups that stayed behind the companies allowed them to envisage the new “competitive market” as a marketplace for big corporations in the form of “managed competition” (Lehman and Weisman 2000). The mainstream theories with claims about social benefits from economies of scale, problems of bottlenecks and sunk costs, the necessity of efficiency, welfare maximization and so forth, have been useful tools to support the chosen methods of the reform.

The reasons to adopt the alternative based on the de-concentration and break up of large corporations were, at least, not worse than the reasons to embrace the approach aimed to the concentration of economic power at the global scale. There is no sound ground to believe that the global oligopolies are better suitable for the purposes of fostering innovations, stimulating investments and development of new services, promoting creation of advanced telecommunications infrastructure, while the alternative would be a solution for the competitive market order and for equalization of opportunities for entrepreneurs in the initial stages of the new economy. There was a chance not only to open the industry at once for competition, but also to destroy any links between industry players and regulatory authorities, while the role of the authorities in this case would be significantly reduced.

## 5. Conclusion

The liberalization reforms, that took place at the end of the last century, has been started on the international level and exploited the idea of free trade, but not the aim of de-concentration of economic power. The former concept has been a lucrative endeavor for powerful international groups or for those who was



seeking to extend their economic and political power in new territories, while the real competitive order has always required efforts in both directions. The chance to change the landscape of the industry and to transform this former monopolistic field into a competitive ground for the new economy has been missed, and the current trend towards a global oligopolistic marketplace yields an unprecedented amount of economic power to narrow groups at the global scale.

The presented analysis allows to argue that in those spheres where explanations of public interest theory are not so robust and clear, the more plausible answers might be found in public choice. The recent surge of “liberalization” speaks rather in favor of the hypothesis of vested private interests in the policy and that they have always been greatly covered by the sauce of public interest justifications. “Liberalization”, “deregulation” or “demonopolization” of the industry have never actually signified the literal meaning of these words and have been used in order to legitimately transform public property into private hands and to extend the borders of business empires of the most powerful actors of the global telecommunications market. Of course, it has provided some public benefits, but such benefits in line with the statement of Milton Friedman (2009) that “private monopoly” is “the least of the evils” in comparison with “public monopoly”. The results of the reform indeed introduced the market mechanisms in the industry, but the real free and open market has never been formed, and it is possible to assert that it has never been among the real objectives of the public policy.

The very important conclusion from the analysis above is that the private interests of the most powerful groups have always had immense support from economic theories. The case of telecommunications shows that ideas and understanding of economic phenomena played an important role in adoption of regulatory regimes, and it is apparent that people on the top of the social pyramid have opportunities to pick up and foster those ideas that better fit their private needs. Even promotion of competition might lead to an anti-competitive outcome when the state tries to achieve this goal through regulation of the market process in accordance with prevailing theories of contemporary economics. The alternative approach, that in different forms might be found in contemporary pro-market non-orthodox theories, is to regulate a form but not a process. According to this outlook economics should not focus on the task of optimal resources allocation, but on the market process and institutions that facilitate this process (see, e.g., Buchanan 1964). If the concentrated form is unable to provide expected results, we have to give a chance for competition; and, moreover, there are obvious reasons to anticipate that a de-concentrated form of the industry will positively affect the landscape of related industries and create opportunities for innovation activity in different fields at the same time.

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