OTT ARE UBERS AND ECS ARE TAXIS. OR NOT?

By Raymundo Enriquez & Gerardo Calderon[1]

I. INTRODUCTION

It is often the case that laws need to catch up with new developments in the world. Technology is certainly not the exception, as today's laws seem at times to be behind the curve. We have recently seen how established operators and regulators around the world face great challenges introduced by digitalization. The most complex of these being whether it is appropriate to frame new services into regulation geared towards already established technologies and if this is the best way to protect consumers and competition.

In this article, we briefly discuss the views of actors from the established Electronic Communication Services ("ECS"), who generally support regulating services, and views from new Over-The-Top ("OTT") services providers, who argue against being subject to such regulations.

We also focus on the disruptive effect that OTT services have on the telecoms sector and the approach of regulators in dealing with these effects. Finally, we compare other industries that had, or are experiencing, similar effects.

II. WHAT IS AN OTT SERVICE?

OTT services deliver media content (i.e. audio, video, text, images, etc.) over the internet and bypasses traditional distribution (i.e. broadcast, radio, written publications). Services that

[1] Raymundo Enriquez & Gerardo Calderon head and senior associate of Baker & McKenzie's Antitrust & Competition Practice Group in Mexico, respectively.

come OTT are typically related to media and communications and are at lower prices since they face very little, or much lower, costs than those that have to be borne by the actors in traditional methods of delivery. OTT services providers rely on Internet access providers for the technical transmission of the offered content. The following are examples of OTT services or applications for a regular user of the Internet: streaming video (e.g. YouTube); videoconferences (e.g. Skype or FaceTime); audiovisual on-demand content (e.g. Netflix, Claro TV, etc.); messaging services (e.g. WhatsApp, Line, etc.) and social networks (e.g. Facebook, Twitter, LinkedIn, Waze). These services require a terminal device with Internet access, like a mobile phone, tablet, TV or videogame console. In essence, any service that users are receiving over the Internet that is not provided directly by Internet Service Providers ("ISP") could be considered an OTT service.

The key point of all of this is that OTT services do not come from the traditional telecoms or Internet service providers, rather these established operators are merely providers of the IP connectivity. The OTT apps ride "on top" of that Internet connection.

From a legal standpoint, it is not easy to find a definition of OTT services to date.[2] In Mexico, the Federal Telecoms Law ("FTL") does not provide a definition or these services, nor does the Federal Institute of Telecoms ("Ifetel"). Ifetel has issued a formal criterion specifically addressing this matter, although it has considered OTT services when analyzing concentrations and issuing resolutions dealing with the telecoms industry.

III. OUR VIEWS

The asymmetries in the cost structures between the different actors (i.e. ECS and OTTs) can be addressed from a regulatory standpoint – i.e. recognizing a different regulatory approach to different technologies – or can be analyzed from a competition standpoint, by determining if the new and the old really belong to the same relevant market. Either approach may fall short from an adequate and sustainable response.

From a competition perspective, it is arguable that disruptive technologies have characteristics that are not substitutes for the ECS's service. These OTT applications are often free of charge for consumers and rely heavily on established infrastructure that is not charged to the supplier of the new type of services. The ECS hence suffer the costs of heavy regulation, infrastructure maintenance and sometimes licensing expenses. Thus, their complaints on what is perceived as unfair competition from the OTT service providers. Furthermore, in many cases, the OTT service providers rely on the infrastructure that the ECS have to maintain. So, if the regulation does not provide for viable ECS models, what impact will this have on the trendy and cheap OTTs? The big question is whether this is a problem of regulation or competition or both?

One could think that OTT services are the Ubers in the telecoms industry, whereas ECS are taxis facing new, potentially competing services. But how close is the substitution

[2] The Body of European Regulators of Electronic Communications ("BEREC") defines these services as "content, a service or an application that is provided to the end user over the open internet." BEREC classifies OTT services into three groups: services that already qualify as an ECS, i.e. services that allow for calls to the publicly available telephone service ("OTT-0"); communication services that compete with ECS on end markets such as instant messaging and voice telephony ('OTT-1"); and other internet based services that do not compete with ECS such as social networks, search engines or online trading facilities ("OTT-3").

between these services both from the supply and demand side? How should OTT services market(s) be defined? These questions, among others, remain to be fully answered.

The lines between OTT services and ECS are becoming increasingly blurred, especially in certain services (i.e. text messaging and telephone services). However, there are also differences that remain clear. For instance, the regulatory framework in Mexico, where, similar to Uber, OTT services providers are less regulated than ECS. The latter must have a license granted by the government to operate, whereas OTT services operators are exempted. ECS have obligations related to price registration, quality of service levels, portability requirements, territories served, among others, while the former does not face such obligations. Notwithstanding, from the end user's perspective it seems, as with the Uber services, some of those differences appear to be more formalistic than real in some cases.

Regardless of the above, IFT has decided that OTT services, specifically video streaming services, will not be regulated under the same terms as traditional Pay-TV services. By following this approach, the debate about the impact of OTT services remains in terms of leveling the playing field. The main concerns are related to the challenges faced by traditional ECS with the expansion of online firms offering products which end users increasingly see as alternatives to their offerings.

The question is if such expansion would result in forcing ECS to exit the market, as it happened for instance to other potential competitors of OTT services providers (e.g. Blockbuster which closed all its stores, presumably after being unable to face competition from OTT providers like Netflix). This would hardly be the case for ECS, as OTT services providers need them, at least as an input for their own services.

OTT services are one of many pieces of the rapid technological progress and growth, generating tremendous benefits for consumers. Even in countries where incumbents historically faced no or very limited competition, prices for digital services have fallen rapidly in recent years. The key element for this progress in our view is the increased convergence of services, although technology and regulation/deregulation have also had an important impact.

All of the foregoing result in digital markets being dynamic, where both new and existing companies have powerful incentives to invest and innovate. The days when consumers were supplied by at least two telecoms providers, for mobile and fixed services and in some cases by additional providers for Pay-TV and Internet services are almost gone. In today's highly competitive environment ECS providers put together bundled services to satisfy all telecoms needs from customers, including OTT services in many cases (i.e. Televisa, once considered dominant in Pay-TV services, has recently launched Blim as part of its offer in response to competitive pressure from Netflix. Another example is mobile services which now include OTT services like Whatsapp and Facebook in some bundled offers).

While undoubtedly digital convergence benefits consumers, it also creates complex challenges for regulators. For instance, the need of implementing enough flexible regulations to avoid distortions generated by outdated or obsolete rules. If regulators fail in this task, for instance by not eliminating discriminatory or static regulations, markets can become distorted and competition will be harmed.

In Mexico, the current FTL introduced relevant changes that aim to deregulate, or regulate more efficiently, rules for services providers (although further changes might still be

required). Specifically, now all telecoms services providers (at least those ECS), are able to incorporate services to a single license, rather than being obliged to request different licenses for each service. Before digital convergence, ECS providers and services operated independently from each other: fixed telephone and mobile services had one function, Pay-TV, etc. It therefore made sense to regulate them separately, under different legal frameworks.

The telecoms market is facing deep changes in the way its consumers interact, entertain and work. Bundling today incorporates two-play to five-play offers. But that alone is not enough to rule the market, when the new reality is OTT services.

Many large ECS are currently exploring new vehicles at the level of media and entertainment as well as on-line digital lifestyles as an initial set of service priorities. In order to generate an attractive offer for consumers, operators should find a way to aggregate OTT services to their service portfolio either through active partnerships or, where appropriate, by acquiring service capabilities.

It has always been clear that consumers love TV content, but they now want the mobile, flexible, personalized and relatively low-cost service of on-demand service offered by OTT services providers like Netflix. They simply do not like the linear TV experience anymore, where channels present programs only at particular times on non-portable screens.

The Netflix success story is well known, which has not been an exception in Mexico, even facing the obstacle of the relatively low penetration of broadband services. Another success story of fast growth, and possibly more similar to the Uber-taxi case, is Whatsapp, which is used by nearly every mobile services user with a smartphone. Among those users, SMS services are rarely used.

OTT services are forcing a recalibration of telecoms services and raising the bar for customer loyalty and retention and service development. We already mentioned that Televisa has launched Blim in response to competitive pressure from Nexflix. America Movil, the dominant ECS provider in Mexico, has also launched its video-on-demand service called Claro Video. All the available options of its Infinitum bundled offers include Internet, voice services and unlimited access to Claro Video. America Movil's OTT offer includes both a free video-on-demand catalogue and a pay-per-view catalogue of more recent movies.

Determining whether the provision of free OTT services may raise competition concerns, and is detrimental to the development of the telecoms markets, is essential in view of their fast growth and penetration. Telecoms markets are typically dynamic and fast-moving. In these circumstances, dominant positions may not be enduring and therefore it is unlikely that OTT services generate competition concerns by themselves.

In addition, and although there seems to be evidence to conclude ECS and OTT services do compete between them, we can also see these services as complementary. While OTT services benefit from broadband networks, ECS also benefit from increased demand for bandwidth driven by OTT services, generating an auto-sustainable system.

IV. CONCLUSIONS

There is no doubt OTT services have introduced additional competitive pressure to ECS and

the traditional telecoms services landscape, as Uber did in the transportation services market to taxis. However, there is no conclusive evidence that ECS and OTT services do compete directly, not only from the supply side, where apparently more differences can be found, as in the Uber-taxi case, but also from the demand side, where there are also arguments to consider ECS and OTT services as complementary services (which is not the case for Uber and taxis).

The above is more or less true depending on the OTT service under analysis. As discussed, Whatsapp appears to be in more close competition with SMS than Netflix with Pay-TV.

Regardless of the approach taken, regulators have the responsibility of establishing adequate rules to level the playing field. Given the dynamics of both ECS and OTT services, regulations should not be discriminatory or static, but rather flexible enough to avoid distortions and hopefully guarantee sustainability.

In Mexico, digital convergence and deregulation efforts by the government (i.e. the current Mexican Telecoms Law, among others) allow competition to increase in the telecoms market. But it is important to anticipate potential anticompetitive effects from the growth of OTT services and ECS providers' adverse reactions or attempts to block new entrants.

If the right approach is taken by both service providers and authorities, there are opportunities for further development of digital convergence and the introduction of additional complementary capabilities between ECS and OTT services.

Based on what has been discussed, our conclusion is that no, OTT services are not the Uber of the telecoms services and ECS are not the taxis. Uber does compete directly with taxis (at least for the user segment which owns a smartphone) and being, in our view, a better service it could potentially eliminate its current, less effective competition. OTT services could be seen as a competitor of ECS. However, the former providers need the later as an essential input to operate.