PUBLIC INTERVENTION IN LIBERALISED MARKETS-

From Regulation to Competition in European Telecoms?

Thesis submitted by Juan J. Montero-Pascual
with a view to obtaining the title of Doctor of Laws of the
European University Institute

Thesis supervisor: Professor Giuliano Amato

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PART I

THE EVOLUTION OF PUBLIC INTERVENTION

CHAPTER 1

INTRODUCTION

SUMMARY: 1.1. Introduction. 1.2. Public Intervention and the General Interest. 1.2. The General Interest in Liberalised Markets.

1.1. INTRODUCTION.

1. Transformations in the telecom sector. During the last two decades, the telecommunications sector has undergone a major transformation. Technology has evolved dramatically forcing the operators to re-formulate their services and to rebuild their networks. Digitalisation has allowed convergence with the audio-visual sector and with informatics, in such a way that dozens of new services have appeared, and the traditional ones have been definitively transformed. Digitalisation, together with the invention of new transmission techniques, such as satellites and fibre optics, has increased the bandwidth, and has forced the operators to renew their networks. These innovations have affected the way most citizens live and work.

Technological progress has transformed the telecommunications services and networks and, at the same time has been one of the main reasons for the transformation of the market structure and of the instruments of public intervention in the telecommunications sector. The influence of the new political order, the lack of public funding for the big investments necessary for the development of modern networks, the need of capital to re-balance the State accounts, or the influence of institutions such as the European Union have also determined the evolution from national public monopolies to open competition between private operators. Public authorities are retreating from the direct provision of the telecommunications services, privatising their networks. At the same time, exclusive rights for the provision of such services are being eliminated, opening the markets to new operators. This is a common trend in most of the sectors in which public authorities monopolised the provision of goods or services, but the telecommunications sector, due to its dynamism, has been one of the first ones to undergo these radical transformations.

Liberalisation, at the same time, is eliminating the instruments of public intervention used traditionally in Europe, due to the fact that the public monopoly is substituted by a competitive market in which even public ownership of one of the operators, if maintained by public authorities, does not allow it to control the market as before. Since these reforms do not exclude public intervention, new mechanisms have to be defined in order for the public authorities to ensure the satisfaction of the general interest. The purpose of the following chapters is to develop the knowledge of these new mechanisms, and their interaction with mechanisms already present but traditionally not applied to the sector, such as the rules on competition.

1.2. PUBLIC INTERVENTION AND THE GENERAL INTEREST.

2. The notion of the general interest. A traditional subject of political philosophy has been the notion of the general interest, its relation with the individual interests, and the role of the public authorities in the defence of such general interest. Two main philosophical as well as political traditions can be identified.[1]

On the one hand, what could be called the common interest tradition, accepts and promotes the harmonic interaction of individual interests for the definition and defence of the general interest. The role of the public authorities would be to provide formal channels for the harmonic definition of the common interest, in order to avoid the illegitimate imposition of a particular private interest.[2]

On the other hand, the public interest tradition transcends the intrinsically negative private interests, and attributes to public authorities the role of defining and protecting the general interest from the illegitimate private interests.[3]

Early precedents of both traditions in relation to the defence of the general interest can be found in the feudal structure of the European societies, both in England and in the continent. The different political evolution of the UK (and

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[1] See RANGEON, F. (1986): "*L'idéologie de l'intérêt général*", Economica, Paris.

[2] This philosophical tradition has been built by authors such as Locke, Adam Smith or Stuart Mill, and can be traced in early philosophers such as Aristotle. See for instance, Aristotle: "*Il est imposible qu'elle [la cité] soit heureuse toute entiere si la plus part de ses elements à defaut de tous, ou du moins certains d'entre eux no possèdent pas le bonheur*", ARISTOTLE, La politique, II, 5, 1264 b 17.

[3] Authors such as Hobbes, Montesquieu and Rousseau have led this approach, that also has ancient precedents such as the writings of Plato. See for instance Plato: "*L'art politique véeritable ne doit pas se soucier de l'intérêt particullier, mais de l'intérêt public*", PLATO, Lois, IV, 875, a.

later the US) and the continent influenced the pre-eminence of one model over the other.[4]

In the UK centralisation of power was limited by the survival of medieval institutions. Private actors were not excluded from the general interest activities, and early precedents developed into the generalised provision of services of general interest by private operators. Public intervention was not excluded, as a derogatory regime was allowed to impose special obligations on private operators subject to judiciary control. Such a tradition was received in the US, where political power was highly de-concentrated (both vertically, due to the federal structure, and horizontally, due to the strict system of balance of powers), and even weak in the frontier territory.

Public intervention in defence of the general interest adopted indirect mechanisms in order to control the activities of the private operators. By the beginning of the 20th century a whole model of indirect intervention through the definition by independent specialised agencies of specific legal obligations to be imposed on the private operators for the fulfilment of the general interest was established. An interesting particularity was what has been called the "unbundling" of the general interest,[5] as the independent agencies were usually assumed to be competent for the evaluation of very precise aspects of the general interest in a particular sector, independently of other considerations. At the same time, instruments such as the antitrust rules were introduced to avoid the concentration of private economic power, as it was understood that such power was a menace for everyone's freedom.

In parallel, in those countries where power tended to be concentrated in the hands of an absolute Monarch, private operators tended to be excluded

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[4] See AMATO, G. and LAUDATI, L. (1999): "When the Economy is Affected with a Public Interest. The protection of Public Interest and Regulation of Economic Activities", in *"The Anticompetitive Impact of Regulation"*.

from general interest activities, and early precedents of public provision of public services developed into the general rule. This was the case particularly in France, where the 1789 Revolution strengthened this process. Public administration centralised the decision-making process as regards the public interest, excluding private actors.

By the beginning of the 20th century, public service became the legitimising title and the limit to public intervention and Administrative Law, in such a way that private operators were excluded from the provision of public services. The consideration of the general interest requirements was concentrated in the public administration in such a way that different aspects were considered simultaneously. The interventionist model nevertheless did not eliminate the mutual interference between public political power and private economic power, and the joint consideration of different public interests reduced the transparency of the process.

3. Public intervention models. Public intervention is closely linked to the notion of general interest. As it has been pointed out, two different conceptions of this notion have traditionally been opposed to each other, and as a consequence, two different models of public intervention for the defence of the general interest have coexisted.

.On the one hand, the general interest can be perceived as the interest of the collectivity, different and incompatible with private interests, which have to be excluded from the definition of the public interest. The direct provision by the public authorities of the goods and services considered of general interest, and therefore, the exclusion of private actors in these sectors, is based on this notion of general interest.

[5] *Ibid.*

Direct intervention usually excludes the effectivity of the free market mechanisms for example through the granting of exclusive rights and therefore the creation of monopolies. The same effect can be reached through interventions which introduce different elements that modify in such a way the development of commercial transactions, for example fixing prices and quantities of production of a certain product, that free market mechanisms are substantially denaturalised. This kind of intervention can be named as *market substitutive intervention.*

On the other hand, the general interest can be perceived as the result of the fair combination of all citizens' private interests. Even if the common interest would be superior to the private interests, the later should be considered legitimate and even necessary for the correct formation of the common interest. Departing from this point, public intervention for the defence of the general interest understood as the common interest is mainly devoted to the control of private actions in order to ensure that private interest are fairly combined, and no private interest is imposed on the community.

Indirect public intervention is generally based on this notion of general interest. The role of public authorities is to ensure the fair combination of private interests in the market. This has been the traditional model of public intervention in the USA, where the provision of goods and services of general interest was entrusted to private operators, controlled by public authorities through the imposition of legal obligations.

This kind of public intervention has the objective of complementing the free market mechanisms for the fulfilment of different objectives not ensured by the market, or even for the protection of the market itself. Public intervention relies on the efficiency of free market mechanisms and limits itself to introduce new elements which according to the internal logic of the supply and demand mechanisms, will lead to the fulfilment of the different objectives.

This kind of public intervention can be named *market complementative intervention*.

4. Market substitutive intervention. Market substitutive intervention models, characterised by the elimination or denaturalisation of the supply and demand mechanisms of the free market economy, can have two origins. On the one hand, public intervention can have its origin in a conscious strategy. Public authorities can impose this kind of intervention due to the lack of confidence in the free market. This lack of confidence can have political reasons. Public authorities can consider that some activities and sectors are of particular importance for the security or well-being of the citizens, in such a way that it is not appropriate to leave to private actors the price fixing and wealth distribution according to the free market mechanisms.

The lack of confidence can also have economic reasons. There are cases in which competition between different actors for the provision of a particular good or a service is not efficient. The theory of the natural monopoly is the best example. Economic theory sustains that there are markets where a monopoly is the most efficient market structure, since economies of scale are so important, that the main producer will always have lower prices, and therefore, the tendency to become the only producer. Public authorities can define a legal monopoly to avoid useless competition in such markets, or even exclude private activity in such markets and provide directly the service, in order to avoid abuses by the private monopolist.

The conscious strategy to eliminate or denaturalise free market mechanisms can derive not so much from a lack of confidence in such mechanisms, but from pressure from different groups hoping to achieve their own private goals.

On the other hand, substitutive intervention can have its origin in a political decision to complement the market that, without desiring such an

effect, modifies in such a stand the free market mechanisms that they are denaturalised.

Substitutive intervention has been the traditional model of public intervention in the telecommunications sector. Even if originally there was limited competition in most of the national markets, it was eliminated in virtually all the States. European and Latin American states opted for the monopolisation of the sector and the direct provision of the services by public administration, excluding any intervention of the free market mechanisms. Prices were fixed by public authorities so that the service would facilitate an income to the budget, and the expansion of the networks was dependent on the public funding availability and the political priority granted to the sector at a particular stage. Public monopolies were created in most of the nations due to political reasons. The influence of the existing structures for post and telegraph services, the military uses of the telecommunications, and the desire to control a facility with an obvious effect on society recommended the elimination of private actors in the sector and the provision of the services directly by the public authorities.[6]

In the US, competition was common for a long period, but by the beginning of the century the most important company (the Bell System) managed to convince the American public authorities to allow the monopolisation of the market by a private company subject to regulatory control by an independent agency. In this case, the interest of a powerful company managed to create a public intervention that avoided the interaction of the free market mechanisms. The Bell System became substantially the sole provider of telecommunications service in the US. Market mechanisms were denaturalise by public intervention obstructing new operators' access to the

[6] *Vide infra* Chapter 3. Nationalisation and Liberalisation of the European Telecoms Markets.

market, and by public price fixing ensuring a fair return to the monopolists' investments.[7]

As a result, free market mechanisms were eliminated from the telecommunications sector in most of the world, and a substitutive public intervention was introduced to rule it. This intervention seems to have responded rather to private interests or to a philosophy of public intervention than to arguments such as the existence of a natural monopoly, or the benefits of a monopoly for the achievement of a universal network, that were only introduced at a latter stage, when public intervention was being challenged.

5. Market complementative intervention. Market complementative intervention by public authorities is based in the general confidence in the interaction between private operators in the market for the satisfaction of the general interest. This kind of intervention is directed to the protection of the market mechanisms themselves, or to the introduction of elements that, following the demand/supply mechanisms, will ensure the fulfilment of some objectives defined by the public authorities.

This intervention can be based in the existence of some market failures, such as the existence of externalities that can be dealt with through the introduction of some elements that force the market to take them into account. Political reasons or the defence of private parties' interest can impose the achievement of certain objectives foreign to the market. For example, it can be convenient to lower the price of a good or a service, or ensure that all the citizens have access to it. This can be achieved through mechanisms complementary to the market that do not obstruct its functioning.

Complementative intervention is subsidiary, in the sense that, in principle, it only takes place when the market itself is not enough for the

[7] *Vide infra* Chapter 2. Regulation and Deregulation of the US Telecoms Markets.

achievement of a particular result. Public administrations introduce very concrete obligations or prohibitions, very often applied to particular cases.

The reform of the telecommunications sector that has taken place in the last decades in most of the countries of the world, is heading towards the creation of competitive markets in the sector, and the substitution of public control of the sector, by the control exercised by the free market mechanisms. The most important element of the reform has been the elimination of the exclusive rights, and the opening of the market to new actors. This reform has usually been accompanied by the privatisation of the facilities that were in hands of the public administrations. The elimination of the monopolies and the privatisation of the public operators, nevertheless, do not entail the elimination of public intervention in the sector, but it certainly requires a modification of the traditional intervention mechanisms in Europe. Market substitutive intervention is being replaced by market complementative intervention, forcing public authorities to define new instruments compatible with the market.

1.3. THE GENERAL INTEREST IN LIBERALISED MARKETS.

6. Public intervention in liberalised markets. During the last decades, the role of public authorities in the economy has been questioned. Market substitutive intervention has been heavily criticised for its lack of efficiency and its tendency to diverge from the objectives originally planned. According to these views, public authorities with limited information and a broad range of interest to defend, cannot ensure an efficient intervention. For these reasons, market substitutive intervention is disappearing, giving place to competitive markets, where public intervention is limited to complementative actions. The telecommunications sector has led this process of reform all over the world.

The transition from market substitutive intervention to competitive markets with complementative intervention is, nevertheless, complicated.

Different factors, including the presence of the traditional monopolist, complicate the development of competitive structures, which do not usually appear in a short period of time. This is particularly the case in those industries characterised by their high barriers to entry (for example the network industries such as telecommunications, energy, transportation etc.) due to the amount of the investment needed, the existence of economies of scale or other reasons.

These difficulties create a transitory period in which traditional market substitutive instruments have been eliminated and thus, cannot impose controls to avoid abuses and, at the same time, the lack of effective competition makes impossible the control exercised by the free market mechanisms, in such a way that private actors, especially the incumbent, might enjoy a private monopoly subject to no control. This lack of control can result in the operator abusing of its suppliers and clients, and, furthermore, in practices aimed to the elimination of the new operators accessing the market. This is particularly dangerous, because it could obstruct the development of competitive structures in such a way that the private uncontrolled monopoly could extend in time its position.

In response to this new situation, a transitory intervention might be necessary. The role of this intervention would be, first of all to control the behaviour of the private actors in the market, in order to impose the necessary obligations and prohibitions to avoid the abuses that the lack of competition allows. This is an intervention that has a lot of instruments in common with the lightest kinds of substitutive intervention, but it is of a different nature, since these instruments should not obstruct the development of the necessary competition in the market.

At the same time, most of the States have opted for a more interventionist approach, and taking into account that some kind of intervention is needed in order to avoid abuses during the transition to effective competition. This intervention could in parallel foster the development of such competition. Public intervention, which should not obstruct the development of

competitive structures, could even facilitate that development. The main instrument of this intervention has been the development of asymmetric obligations, lighter on the new entrants and heavier on the incumbent.

This asymmetry allows for the satisfaction of both objectives of the public intervention during the transition period. Firstly, it allows the abuses derived from the excessive market power of the operators with significant market power to be controlled. It is not necessary to impose these obligations to the new comers, because their weak position makes it impossible for them to commit these abuses. Secondly, the existence of a lighter regulation should allow new comers to grow bigger and faster in a shorter period of time and in such a way that they will be able to impose market pressure on the incumbents.

This kind of intervention is particularly complex. First of all, in the European case it requires a major reform of the instruments and institutions of intervention. Secondly, a delicate balance is required so that public intervention facilitates the development of competition without encouraging the entrance of inefficient operators.

The telecommunications sector has, once again, led the apparition of this new kind of intervention. The existence of important barriers to entries due to the investments required for the development of telecommunications networks, the importance of the network externality, and the existence of enormous economies of scale, inhibit new comers' access to the market and their development into effective competitors. The former monopolies enjoy strong dominance in a market difficult to control with the general instruments.

7. Instruments of public intervention. Demonopolisation and privatisation have eliminated the most important instruments of public intervention in some sectors, including the telecommunications sector. Direct intervention of public authorities is being substituted by free market mechanisms, but these reforms do not modify the fact that these sectors are

characterised by a general interest in the efficient and economic provision of the services, due to the role of basic industries, fundamental for the development of general economic activity, and their effect on the general population's standards of living. For these reasons the control by the public authorities is recommended for the satisfaction of the general interest as well as the intervention in those cases in which the free market mechanisms do not ensure such objectives. Public intervention, therefore, is subsidiary and complementative of the market forces.

In the framework of the liberalised markets, there are two main general horizontal instruments of public intervention. On the one hand, there are the rules on competition, which protect the competitive structure of the market so that free market mechanisms can effectively control the activity in the market of all the actors. On the other hand, we find the rules on consumer protection, introduced in order to protect consumers against the abuses of the product and service providers. A third instrument of public intervention is sector specific regulation. This instrument provides specific tools for public intervention in order to complement the free market mechanisms and the horizontal instruments of intervention.

Competition Law provides a public intervention instrument for the protection of free market mechanisms. This is particularly important in the de-monopolised sectors where competitive structures are developing and therefore are very weak. A strict application of the rules on competition in these sectors will allow the developing of competitive structures and avoid some of the abuses derived from the market power of the incumbents. The special situation of these markets can require at times a special application of these rules, but this adaptation should not modify the basic principles of the norms.

The general rules on consumer protection impose on operators various obligations aimed at obstructing abusive behaviours caused by the contractual asymmetry between large corporations with their thousands or millions of

clients, and individual citizens. Such rules can provide efficient mechanisms of protection against the abuses of the incumbent operators in a period in which no effective constraints are imposed by a non-existing competition in the market. Nevertheless, consumer protection rules do not provide mechanisms to foster the elimination of the market power, and therefore they seem insufficient to protect consumers' interest in the long run.[8]

Sector specific regulation has a double role in the liberalised sectors. On the one hand, it is the right ambit for public intervention in the direct defence of the general interest. Once the public authorities define an objective of general interest, it is their obligation to check whether market mechanisms are enough for the satisfaction of such objective. If this is not the case, complementative measures should be introduced without obstructing the functioning of the market. This complementary intervention can be temporary, but on occasions market failure can be consistent and require a permanent intervention of the public authorities. This public intervention should not obstruct competition, and, in the transitory phase to effective competition could even introduce some asymmetries to facilitate such transition.

On the other hand, sector specific regulation can be introduced in de-monopolised sectors during the transitory phase towards effective competition with the intention of accelerating such transition and, at the same time, avoiding the abuses that the lack of competition allows to those operators with significant market power.

8. Competition Law in the telecommunications sector. Traditionally, competition Law plaid a very limited role in sectors where public authorities defined exclusive rights for the provision of services of general interest. This

[8] The study of the consumer protection rules in the telecommunications sector and the interaction with the other instruments of intervention is outside of the scope of this thesis, which is focused on the interrelation between the rules on competition and sector specific regulations. Some references to these rules will, nevertheless, be introduced in the following pages.

was the case not only in the European Union but also in the US. The situation changed drastically and different reasons carried to the application of competition Law to these sectors, and specifically to the telecommunications sector. This put an end to the exclusive rights in the European Union and the US. Even if the role of competition Law in the de-monopolisation of the sector was relevant, it was neither the only factor nor the sole instrument. What is clear is that the rules on competition have been increasingly important and, for sure, will play a fundamental role in the following years.

The coexistence, in the European Union of Community and national legislation on competition Law means that different institutions apply different, even if similar rules. This introduces an element of confusion in the application of competition Law in the telecommunications sector. Nevertheless, the existence of this double level facilitates a very interesting mechanism such as the application of competition Law not only to private companies and even public companies, as in many States, but also the application of competition Law directly to public authorities that adopt measures whose effect is contrary to the rules on competition defined in the Treaty. These interesting mechanisms have allowed the liberalisation in Europe and, at the same time, introduce an element of pressure for the Member States in the process of transition to effective competition.

Although the application of competition Law might have been one of the legal instruments which has allowed the elimination of exclusive rights in the sector, and even if competition Law has an important role in avoiding agreements and unilateral actions that restrict competition, the role of competition Law in recently monopolised markets is necessarily limited. In these markets where no effective competition exists due to the existence in the recent past of a legal monopoly and the weakness of the new comers, competition Law can obstruct the anticompetitive behaviour of the incumbent with the objective of prolonging its dominant position or even eliminating the

existing competition. But it has to be affirmed that competition Law does not have the instruments to create competition in those markets where it does not exist. Competition Law was designed for the protection of competition, but not for the creation of such competition. Furthermore, the rules on competition are not the bestinstrument to govern markets with failures that limit the level of effectiveness of competition.

9. Sector specific regulation in the telecommunications sector. It has been pointed that competition Law may not ensure the satisfaction of all the general interests in the telecommunications sector. It is for this reason that sector specific legislation has been passed and specific institutions have been created in most of the States where the sector is being liberalised.

Sector specific regulation has two major objectives. On the one hand asymmetric legislation has been passed for the promotion of competition. Particularly important is the regulation of interconnection, as well as the regulation of prices. On the other hand, legislation has been passed for the direct defence of certain interests, such as the universality of the basic telecommunications services, the efficient management of scarce resources, and the definition of obligatory basic quality standards. In the European Union, most of this legislation has its origin in Community Directives.

Specific institutions have been created in most of the Member States for the application of the new legislation. Most of these institutions have adopted the form of independent commissions following the model of the independent regulatory authorities of the US. These commissions create problems of constitutionality in most of the Member States, due precisely to their independence from the executive power and, indirectly from the legislative.

Sector specific regulation is a concentrated and continuous control of a specific economic sector through the imposition of legal obligations on the private actors in the sector. Even if there are certain general obligation to do or

not to do, this kind of public intervention is characterised by the adaptation of the general principles to each actor in the market, in such a way that a very specialised and independent institution is necessary for the development of the intervention. Specific obligations are defined originally in the title of access to the market. Other obligations can be defined as and when necessary.

10. Conflicts and balances. Competition Law and sector specific regulation are the two main types of public intervention in the telecommunications market, and are developed by different institutions at a national level as well as different services of the European Commission at a Community level. Conflicts between the different institutions and the different levels of intervention are inevitable. Those conflicts are not limited to the exercise of power between different institutions, but are conflicts which reflect the tension between different kinds of public intervention.

Sector specific regulation requires the conceptualisation and materialisation of public intervention mechanisms for the direct defence of the general interest, in particular mechanisms devoted to ensuring that basic telecommunications services are offered at an affordable price to all citizens, independently of their location in rural areas. Community Directives have defined a universal service scheme for the most fundamental services. The fulfilment of the general interest, which is the objective of this scheme, is the provision of basic services to all the population without introducing obstacles to the development of competition in the sector. Member States are obliged to comply with the obligations in the Directives, and regular mechanisms will apply in case Member States do not implement these obligations in the right way.

Nevertheless, schemes that are supposed to be subsidiary, complementative, and compatible with effective competition in the market, can be developed in such a way as to obstruct competition. In this case, sector

specific regulation for the direct satisfaction of the general interest can conflict with the rules on competition defined in the European Community Treaty.

Even if Community competition Law, specifically Articles 81 and 82 of the EC Treaty (former Articles 85 and 86), was established to prevent anticompetitive measures adopted by undertakings, different mechanisms allow the Commission to obstruct public measures with anticompetitive effects. Article 86 EC Treaty (former Article 90) and the *effet utile* doctrine allow the Commission to initiate procedures against regulatory measures of the Member States with anticompetitive effects. In such a way, the Commission can obstruct universal schemes that unnecessarily distort the competitive process.

As I argue later, intervention for the promotion of competition tries to complement market mechanisms, imposing upon the incumbents the pressure that effective competition would impose, plus a little more in order to modify the balance existing in the market. These obligations are closely connected to the obligations imposed by competition Law and a certain correlation can be observed. The point is that sector specific regulation advances the line of intervention with respect to competition Law, in order not only to protect competition but also to promote it. Since competition Law is insufficient, sector specific regulation has been adopted temporarily to obtain these objectives.

In principle, sector specific regulation for the promotion of competition imposes *ex ante* the obligations that competition Law could impose *ex post*. In this way, the abuses that the extraordinary market power of the incumbent makes more probable, are avoided before they take place. Sector specific regulation also avoids the cumbersome procedures and problems of proving certain abuses. At the same time, sector specific legislation imposes certain obligation outside of the scope of the rules on competition. These are

particularly those obligations that impose tougher asymmetric conditions not only for the protection of competition but for its promotion.

The key is to avoid the application of competition Law in those issues related to the promotion of competition for which the rules on defence of competition were not created. This could denaturalise them and create distortions in their application to other sectors. At the same time, the application of sector specific regulation for the promotion of competition should be restricted to those markets where effective competition is lacking, thus avoiding the over-regulation of those markets with a certain degree of competition.

The purpose of these pages is to shed some light on the relation between sector specific regulation and competition Law. Departing from their evolution and the study of their characteristics, strengths and limitations, I will examine how both instruments of public intervention complement and counterbalance each other.

CHAPTER 2

REGULATION AND DEREGULATION OF THE US TELECOMS MARKETS

SUMMARY: 2.1. The Origins and Evolution of Economic regulation. 2.2. Origins and Evolution of Antitrust. 2.3. The Process of Deregulation. 2.4. Public Intervention in the US Telecommunications Markets. 2.5. Conclusions.

2.1. THE ORIGINS AND EVOLUTION OF ECONOMIC REGULATION.

11. Early precedents of the regulatory intervention. It is of great interest to trace the origins and evolution of both of regulation and antitrust. Both instruments of public intervention appeared as political responses to the challenges faced in the US due to industrialisation in the 19th century, but have their roots in early Common Law.

Between the 13th and 14th centuries, a new institution appeared, the "common calling",[9] a category of professionals and craftsmen that provided their services for the general public as a business. In feudal England, this kind of activity was an object of suspicion, and for this reason was subjected to a strict legal regime. On the one hand, a special liability regime was imposed.[10] On the other hand, special obligations were also imposed on them, such as the provision of their services to everyone requesting it under reasonable circumstances, the obligation to provide the service adequately and, after the Black Death of 1348, the obligation to provide their services for a reasonable price.[11]

Economic growth and change in the social structure of society led to the popularisation of "common callings". By the seventeenth century, professionals offering their services to the general public were common. At the same time, the general assumption of liability of the provider of a service was extended to every contract. In this way, suspicion, as well as the legal difference that separated the legal regime of the private from the "common calling" disappeared, and with them, the special obligations to charge a reasonable rate

[9] This institution was object of a number of studies at the beginning of the century, when the first regulatory agencies were created. For the development of the concept of "common calling" and "common carrier", and their connected obligations, see ADLER, E. (1914): "Business Jurisprudence", in *Harvard Law Review*, vol. 28, pp. 135-162; BURDICK, C. (1911): "The Origin of the Peculiar Duties of Public Service Companies", in *Columbia Law Review*, vol. 11, pp. 514-531, 616-638, and 743-764; McALLISTER, B. (1930): "Lord Hale and Business Affected with a Public Interest", in *Harvard Law Review*, vol. 43, pp. 759-791; STONE, A. (1991): "*Public Service Liberalism. Telecommunications and Transitions in Public Policy*", Princeton University Press, Princeton NJ; and WYMAN, B. (1904): "The Law of the Public callings as a Solution of the Trust Problem", in *Harvard Law Review*, vol. 17, no. 3, pp. 156-173, and no. 4, pp. 217-247.

[10] In medieval England contracts between individuals for the provision of services did not include the liability of the provider in case of damages to the other party's property, unless a particular clause (called *assumpsit*) was included in the contract. In the case where the provider was a "common calling", the assumption of liability was automatic, without the introduction of the liability clause in the contract. *Ibid.* WYMAN (1904), p. 157.

[11] The obligation was defined in the 1439 Statute of Labourers, *vide* STONE (1991), p. 20 (*supra* footnote 9).

and to serve all. There were nevertheless, two exceptions: "common carriers"[12] and "common inn-keepers".[13] These "common callings" maintained the obligation to serve all, to serve in a sound manner, and to charge reasonable rates. The historical origin of the obligations was replaced by public utility reasons, being assimilated somehow to the activity of a public officer, whose charge was to serve the general interest. As stated by the Courts, the "common carrier" "has made Profession of a Trade which is for the Public Good, and has thereby exposed and vested an interest of himself in all the King's Subjects that will emply him in the Way of his Trade".[14] It is because of this reason that all three obligations were maintained. This was the first precedent of how private persons, subject to some obligations, could provide services of general interest for the community.

12. 19th century developments. During the nineteenth century new technologies appeared and developed. Railroads, water, energy and telecommunications became necessary for economic development as well as for raising the standard of living. These activities were soon considered of general interest. The United States led the invention and development of these infrastructures, and therefore was the first country which had to define a public policy in order to ensure the satisfaction of the general interest. Such policy, as it will be shown was based on the English tradition of the common carrier.

From an early stage, certain behaviour of the providers of the new services started to damage the interests of various strong groups. Particularly important was the Granger movement. The grangers of the Mid-West of the US required public intervention against the abuses of the monopolists in charge of transportation systems (such as railroads and channels) and warehouses,

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[12] Persons offering to the general public the service of transportation of people or goods, whether in land or water.

[13] Persons offering the service of accommodation to the general public.

[14] *Lane v. Cotton*, 1701, *vide* BURDICK (1911), p. 520 (*supra* footnote 9).

indispensable for the commercialisation of their products. The strong position of this group required some action by the public authorities.

There were several reasons why the direct provision of the services by the public authorities was not considered. Firstly, there was a long tradition of private persons providing public services in the United States. This did not only include the figure of the "common carrier" but also the incorporation of private companies for the provision of services of general interest.[15] The second reason for the non nationalisation of the industries of general interest was the political structure of the US. The separation of powers both at a horizontal and vertical levels made more difficult the intervention of public authorities in the public service sectors. Lastly, the weak public presence in the frontier territory made direct public intervention impossible.

The lack of appropriate instruments for achieving public intervention forced Legislators and Judges to define new mechanisms. A first line of case-law tried to impose on all the network industries, the regime defined for the "common carrier", based on the content of the activity: transportation. This line was useful for some industries, such as telecommunications,[16] but was more difficult for others,[17] and absolutely impossible for several which did not have the characteristics of a "common carrier".[18] These decisions were based on a

[15] In the 19th century the granting of charters of incorporation to private persons for the provision of services of general interest such as hospitals, schools, roads and even the creation of frontier villages was common. Incorporation would later be granted for the development of business which promoted general welfare (banks, insurance, manufacture) and at the last stage, became the most common instrument of business organisation. See SEAVOY, R. (1982): "*The Origins of the American Business Corporation, 1784-1855*", Greenwood Press, Westport.

[16] "A telephonic system is simply a system for the transmission of intelligence and news. It is, perhaps, in a limited sense, and yet in a strict sense, a common carrier", *Missouri v. Bell Telephone Company*, (1885) 23 Fed. 539, *vide* BURDICK (1911), p. 622 (*supra* footnote 9).

[17] Pipe lines of gas were considered a common carrier, even if the owner only transported his own gas. The service was not provided to the general public, but was considered a common carrier in *Prairie Oil & Gas Company v. United States*, 204, Fed. 798.

[18] "it became necessary to convert into a common carrier an activity which was not of that character under any accepted definition of the term", *vide* ADLER (1914), p. 143 (*supra* footnote 9).

misunderstanding. The special regime of the "common calling" did not derive from the activity of transportation, but from its nature of "trade, which is for the public good".[19]

13. Economic regulation by the States. Economic regulation was initiated by the State Legislators with the approval of the Judiciary. The answer of the State Legislators to the pressure given by the Grangers was the adoption of legal measures imposing obligations upon the private operators active in the new technology markets, particularly with regard to limits on tariffs. Such legislative measures were challenged before the Courts.

The first case on this subject that came to the Supreme Court of the United States was *Munn v. Illinois*. The Illinois constitution defined grain warehouses as a public service. In 1870, the State legislature passed a statute fixing certain obligations applying to warehouses in Chicago, the main one being the obligation to fix permanent rates for one year, publish them and apply them to all their clients without discriminations. The Supreme Court upheld the statute: "Looking to the common law, from whence came the right which the Constitution protects, we find that when private property is 'affected with a public interest, it ceases to be juris privati only'. Lord Chief Justice Hale said this more than two hundred years ago.[20] [...] Property does become clothed with a public interest when used in a manner to make it of public consequence, and affect the community at large. When, therefore, one devotes his property to a use in which the public has an interest, he, in effect, grants to the public an interest in that use, and must submit to be controlled by the public for the common good, to the extent of the interest he has thus created. He may

[19] *Lane v. Cotton, vide* BURDICK (1911), p. 520 (*supra* footnote 9).

[20] In McALLISTER, B. (1930): "Lord Hale and Business Affected with a Public Interest", in *Harvard Law Review*, vol. 43, pp. 159-191, it is demonstrated that those were not the exact words of Justice Hale. English law was not so clear on the subject, but the precedent of the "common carrier" was, nevertheless in that line.

withdraw his grant by discontinuing the use; but, so long as he maintains the use, he must submit to the control".[21]

In *Munn v. Illinois* two requirements were defined for the public intervention: general interest, and concentration in the sector. It was only at a later stage that the case law was refined.[22] In *Nebbia v. New York* the Supreme Court clearly identified the legitimising title for public intervention: "The use of private property and the making of private contracts are, as a general rule, free from governmental interference; but they are subject to public regulation when public need requires. [...] To say that property is "clothed with a public interest", or an industry is "affected with a public interest", means that the property or the industry, for adequate reason, is subject to control for the public good".[23]

Public intervention by the State Legislators was legitimised with the approval by the Supreme Court. The Granger movement not only forced the adoption of State legislation, but it also forced the adoption of a federal statue, the Interstate Commerce Act.[24]

14. Early regulatory agencies. Economic regulation can be defined as the intervention of public authorities in economic activity, usually by specialised independent agencies, through the imposition of specific legal obligations on individual private operators, for the fulfilment of the general

[21] *Munn v. Illinois*, 94 U.S. 113, (1876).

[22] *Munn v. Illinois* was the first important ruling by the Supreme Court on the field, but was followed by others, such as *Budd v. New York*, 143 U.S. 517 (1892), or *Brass v. North Dakota*, 153 U.S. 391 (1894).

[23] "a State is free to adopt whatever economic policy may reasonably be deemed to promote public welfare", *Nebbia v. New York*, 291 U.S. 502 (1934), pp. 523, 525, and 537.

[24] Interstate Commerce Act, February 4 1887.

interest. Different models of regulation can be identified according to the scope and effects of the legal obligations imposed on the private operators.[25]

Some of the public service industries were very complex, and the definition of the adequate quality of their services, or the reasonableness of their prices, was extremely complicated, and could only be checked by a permanent organisation. At the same time, such decisions had a high political content that Courts were not always prepared to face.[26] The effective provision of the services of general interest required a clear definition of the activities "clothed with a public interest", and a decided enforcement of the obligations vested on the private companies providing those services.

By the end of the 19th century, a new intellectual and political movement, the Progressives, launched a debate on the improvement of public policies via the introduction of expertise in the administration and the creation of independent specialised agencies for the regulation of the markets.[27] In this way, public intervention for the protection of powerless consumers would at the same time promote a better exploitation of resources. The adoption of the Sherman Act in 1890 can be identified with this movement.[28]

The creation of the State Public Utilities Commissions between the 19th and the 20th centuries was the result of the convergence of different interest. Firstly, the utopic movement of the Progressives had developed a theory about public intervention through independent agencies. Secondly, political leaders at

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[25] See REAGAN, M. (1987): "*Regulation: The Politics of Policy*", Little Brown, Boston, pp. 17-18.

[26] "I think the proper course is to recognise that a State legislature can do whatever it sees fit to do unless it is restrained by some express prohibition in the Constitution of the United States or of the State [...] Courts should be careful not to extend such prohibitions beyond their obvious meaning by reading into them conceptions of public policy that the particular Court may happen to entertain". Dissenting opinion of Mr. Justice Holmes in 273 U.S. 418, 445-47 (1927), *vide* McALLISTER (1930), pp. 159-171 (*supra* footnote 9). If Justice Holmes considers the risks in the control by Courts of the public service obligations imposed by legislators to public service providers, *a fortiori* the definition by the Courts of the public service obligations was inadequate.

[27] See HORWITZ, R. (1989): "*The Irony of Regulatory Reform*", Oxford University Press, New York.

[28] *Vide infra* Chapter 2.2. Origins and Evolution of Antitrust.

State level adopted this ideology as an instrument to initiate political careers at a federal level. Lastly, the industry agreed with the creation of the State agencies, as it expected that they would be easier to control than the local governments that were already introducing heavy constraints on the operators.[29] The first states to create such independent agencies were Wisconsin and New York. Between 1905 and 1915 over 30 states created their regulatory agency.

The movement of the creation of the regulatory agencies expanded to the federal level. The first agency was the Interstate Commerce Commission, created mostly for the regulation of the railway transportation activities. The compromise that made the Act possible,[30] and the negative attitude of the Supreme Court,[31] made "that Commission a useless body for all practical purposes",[32] but the reforms introduce by the Hepburn Act[33] in 1906 and the Mann-Elkins Act[34] of 1910 strengthened its position. The Federal Trade Commission was created in 1914.[35]

Early regulation by Legislators and the Judiciary was aimed of controlling companies with significant market power, in order to avoid abuses of such power. Public intervention was limited to that which was complimentary to the market.

15. Entry-and-price regulatory agencies. The second wave of the creation of regulatory agencies was the New Deal in the 1930's. The depth of

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[29] See ANDERSON, D. (1980): "State Regulation of Electric Utilities", in *"The Politics of Regulation"*, J. Wilson, Basic Books, New York.

[30] See SCHWATZ, B. (1973): *"The Economic Regulation of Business and Trade. A Legislative History of U.S. Regulatory Agencies"*, Schwatz, New York, p. 18.

[31] In the *Maximum Rate* Case 167 U.S. 479 (1897), the Supreme Court denied the competence of the Commission for maximum prices fixing.

[32] Mr. Justice Harlan in his dissenting opinion in the case *ICC v. Alabama Midland R. Co.* 168 U.S. 144 (1897).

[33] Hepburn Act, June 29 1906.

[34] Mann-Elkins Act, June 18 1910.

[35] Federal Trade Commission Act, September 26 1914.

the recession obliged public authorities to reformulate their policies, and to propose a greater public intervention in economic activity. In this way, five out of the big seven regulatory commissions were created: the Federal Power Commission (1930), the Federal Communications Commission (1934), the Securities and Exchange Commission (1934), the National Labour Relations Board (1935), and the Civil Aeronautics Board (1938).

Entry-and-price regulation, imposed by the big regulatory agencies during the Depression and the New Deal, substituted market mechanisms with the legal rights and obligations imposed by the agencies upon the private operators. On the one hand, in order to ensure stability (and also to protect the existing operators), entry into the market was restricted. A certificate of public convenience and necessity, granted by the regulatory authority, was required for the provision of the service. At the same time, the former obligations of the English common calling were imposed upon the monopolists. The obligation to serve all who apply for the service forced the regulated industry to provide their services also in rural areas, and to build capacity ahead of demand, in order to ensure the provision of the service in exceptional cases. The obligation to render a sound service was specified in the minimum quality and security obligations. The obligations to serve all the consumers on equal terms prevented discriminations.

On the other hand, the regulatory commissions controlled prices. The old abstract obligation of the common calling to charge only a just and reasonable price, became a concentrated control by the regulatory agency. The agency tried to establish an equilibrium between the control of prices in order to avoid abuses by the monopolist, and the right of the monopolist to non confiscatory rates, protected by the Fourteenth Amendment.[36] The fair rate of return of the

[36] See PHILLIPS, C. (1993): "*The Regulation of Public Utilities. Theory and Practice*", Public Utilities Reports, Arlington.

monopolist's investments became the central axis of the regulatory intervention.

The monopolisation of the markets and the price-fixing by the regulatory agencies substituted free market mechanisms with the bargaining mechanisms between the regulator and the regulated industry in the definition of services, prices and qualities.

16. Social regulatory agencies. The last period of creation of regulatory agencies was the period between 1965 and 1977, with the Great Society program of President Johnson. This was the period of the civil rights movement, the Vietnam War, and the movements in defence of minorities, consumers and the environment. The regulatory agencies created during this period were essentially contrary to the industry's interests, since they often introduced the consideration of externalities and the social effects of economic activity. The Equal Opportunity Commission (1965), the Environmental Protection Agency (1970) and the Consumer Product Safety Commission (1972) were created in this period, when, direct participation of citizens and consumers in the administrative procedure of most of the regulatory agencies was also introduced.[37]

Most of the social regulation, introduced in the 1960s, had the traditional aim of solving market failures, in particular the introduction of social rights and externalities into the economic debate. Civil rights, labour rights, and environmental considerations were protected through the imposition of particular obligations on private operators active in the market. Such intervention, nevertheless, did not aim at substituting the market, but rather was seen as a complement to it.

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[37] See, as an example, *United Church of Christ v. FCC* 359 F. 2d 994 (D.C. Cir. 1966) and *Scenic Hudson Preservation Conference v. FPC*, 354 F 2d 608 (2nd Cir. 1965).

2.2. ORIGINS AND EVOLUTION OF ANTITRUST.

17. Early precedents of antitrust. As in the development of regulatory intervention, the roots of antitrust can be found in ancient English Common Law.[38] It is obvious that medieval England was not characterised by the existence of a free market economy,[39] but there are some interesting precedents of the main principles of antitrust.

Firstly, an aversion for monopolies can be identified. The *Statute of Monopolies* of 1623, declared that "all monopolies heretofore or hereafter to be granted to any person or persons, bodies politic or corporate for the sole buying, selling, making, working or using any thing within this realm, or other monopolies, are and shall be utterly void and of no effect and in no way to be put into execution".[40]

Secondly, the principle of freedom of entrance to the market was repeatedly stated. In the *Schoolmasters' Case,* in 1410, the right of a new schoolmaster to initiate activities in a town were two masters were already providing the service was defended, even if it caused some form of economic damage to the existing providers of the service.[41] Thirdly, in the *Salt Makers of Droitwich Case* of 1758 the Court sustained that collusive agreements, and in particular "price-fixing agreements, were of bad consequence and ought to be

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[38] See FOX, E. (1990): "The Sherman Antitrust Act and the World-Let Freedom Ring", in *Antitrust Law Journal*, vol. 59, no. 1, p. 109-118.

[39] The strong presence of the guilds, for example is a prove of the feudalistic structure of such society. Nevertheless, action against the guilds was undertaken earlier than in continental Europe.

[40] See HANDLER, M. (1960): "*Cases and Other Materials on Trade Regulation*", The Foundation Press, Brookling, pp. 46-47, as well as pp. 44-46, for a reference to *The Case of Monopolies*, where the Court of King's Bench, in 1602, considered void a exclusive right granted by the Queen Elisabeth for the import and production of playing cards. Chief Justice Popham considered not only that monopolies damaged those traders that exercise the same trade, but also consumers, since monopolies rised prices, and lowered quality. For these reasons, monopoly was contrary to the Common Law.

[41] *Ibid.* HANDLER (1960), pp. 12-13.

discountenanced".[42] Finally, the definition of reasonable restrictions for the protection of competition was accepted in *Mitchel v. Reynolds*, in 1711.[43]

18. The Sherman Act. During the last decades of the 19th century there was a strong tendency towards large-scale corporate concentration, particularly in such new industries as oil and railroads, but also in more traditional markets such as cotton and sugar. The corporate legislation that prohibited one corporation from holding stakes in another corporation was by-passed in order to allow corporate consolidation through the use of the Common Law institution of the trust.[44] Even if the evolution of corporate legislation would later eliminate such prohibition, the word antitrust would remain as a reference for those public and private movements which were contrary to economic concentration.

The initial antitrust movement was led by the agrarian populists, the Grangers,[45] against the concentration and anticompetitive practices of the railroad and water channel companies.[46] A second stage in this movement saw the urban middle classes, the main supporters of the Progressives,[47] take the lead on the opposition to corporate concentration. Just as the American political tradition was diffident of the concentration of power concentration, the

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[42] The agreement between salt makers to fix a minimum price for their product under an economic penalty was considered contrary to the Common Law, *ibid.* HANDLER (1960), p. 137.

[43] In a case where the leaser of a bake house had broken the compromise not to compete in such business, the Court considered that such kind of compromises would be void if imposed, excessive or if it would result in a monopoly, *ibid.* HANDLER (1960), pp. 105-106.

[44] Individual shareholders of the consolidating corporations tendered their stock to trustees in exchange for trust certificates. The resulting trust was not incorporated and hence was thought to be immune from the limitations of corporation law, see HOVENKAMP, H. (1990): "Antitrust Policy, Federalism, and the Theory of the Firm: An Historical Perspective", in *Antitrust Law Journal*, vol. 59, no. 1, pp. 79-81.

[45] LETWIN (1926): "Congress and the Shermann Antitrust Law: 1887-1890", in *University of Chicago Law Review*, vol. 23, p. 223.

[46] This was also the origin of the regulatory intervention in these sectors, *vide supra* Chapter 2.1. Origins and Evolution of Economic Regulation.

[47] *Vide* the role of the Progressive movement in the creation of regulatory agencies *supra* Chapter 2.1. Origins and Evolution of Economic Regulation.

concentration of private economic power raised concerns, and public intervention was demanded to avoid such concentration.[48] As a result, fourteen States inserted antitrust provisions in their State Constitutions before the enactment of the Sherman Act on July 2, 1890.[49]

The Sherman Act tried to clarify the Common Law principle of illegal combinations in restraint of trade, at the very same time that limitations on the unilateral monopolisation of the markets were introduced.[50] According to the majority doctrine, the main reason given for the approval of such legislation was that it would control of the damaging effects of the concentration of economic power.[51]

19. The evolution of antitrust. The first two decades of enforcement of the Sherman Act were characterised by confusion and lack of sense of direction. The broad language of the Sherman Act did not provide a clear indication for Courts to apply such provisions. The initial literal interpretation of the Act by Courts prohibited "every contract [...] in restraint of trade", in such a way that any contract or agreement which introduced any kind of

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[48] See MILLON, D. (1991): "The Sermann Act and the Balance of Power", in *The political Economy of the Sherman Act: The First Hundred Years*, T. Sullivan, Oxford, pp.85-115.

[49] See MAY, J. (1987): "Antitrust Practice and Procedure in the Formative Era: The Constitutional and Conceptual Reach of State Antitrust Law, 1880-1918", in *University of Pennsylvania Law Review*, vol. 135, no. 3, p. 499.

[50] "Section 1. Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is hereby declared to be illegal. Every person who shall make any such contract or engage in any such combination or conspiracy shall be deemed guilty of a misdemeanour.

Section 2. Every person who shall monopolise, or attempt to monopolize or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several states, or with foreign nations, shall be deemed guilty of a misdemeanour".

[51] "The popular mind is agitated with problems that may disturb social order, and among them nothing is more threatening that the inequality of condition, of wealth, and opportunity that has grown within a single generation out of the concentration of capital into vast combinations to control production and trade and to break down competition", opening speech of Senator Sherman in the Congress debate of the bill, in CAREY, R. (1989): "The Sherman Act: What Did Congress Intend?", in *The Antitrust Bulletin*, vol. 34, no. 2, p. 344. See also AMATO, G. (1997): "*Antitrust and the Bounds of Power. The dilemma of liberal democracy in the history of the market*", Hart Publishing, Oxford.

restriction to trade, even if positive for competition, or any merger would be contrary to the Sherman Act.[52]

A new phase was opened by the Supreme Court when it stated that the Sherman Act had only meant to forbid unreasonable restraints of trade.[53] The introduction of the Rule of Reason required the analysis of the economic consequences of the restraints of trade, but the lack of economic skills of the Courts produced intuitive and speculative analysis of such consequences.[54] Over time, Courts adopted some of the basic principles of the industrial organisation theory in order to analyse market structures. Notions such as oligopoly, barriers to entry, predatory pricing and so on became common in antitrust judgements. A limited number of restrictions, were nevertheless generally considered *per se* a restraint of trade, as was the case for price-fixing.

20. The Chicago School on antitrust. By the end of the 50's, a group of scholars based in the University of Chicago, started to develop studies based on the application of price theory to some antitrust issues such as tie-in, resale price maintenance or predatory pricing. Their results showed that some of the most traditional antitrust categories were incompatible with economic theory.[55] The initial criticism gave place to a whole new theory on antitrust. The point of departure was the clarification of the scope of the antitrust legislation. According to the Chicago School the only purpose of antitrust legislation was to promote consumer welfare.[56] A sound analysis of the effects of behaviours

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[52] See GELLHORN, Ernest (1986): "Climbing the Antitrust Staircase", in *The Antitrust Bulletin*, vol. 31, no. 2, pp. 342-343.

[53] *Standard Oil of New Jersey v. United States*, 221 U.S. 1 1911.

[54] PERITZ (1989): "The "Rule of Reason" in Antitrust Law: Property Logic in Restraint of Competition", in *Hastings Law Journal*, vol. 40, p. 285.

[55] See POSNER, R. (1979): "The Chicago School of Antitrust Analysis", in *University of Pennsylvania Law Review*, vol. 127, pp. 159-182.

[56] In a somehow voluntaristic study, it was even sustained that consumer welfare was the only goal of Congressmen when the Sherman Act was passed in 1890, see BORK, R. (1966): "Legislative Intent and the Policy of the Sherman Act", in *The Journal of Law and Economics*, vol. 9, p. 7 and BORK, R. (1978): "*The Antitrust Paradox. A Policy at War with Itself*", Basic Books, p. 20.

scrutinised according to the price theory would show that most of the practices considered in the past to be restrictive of trade would not have such an effect, at least in the mid-term. The most radical scholars even pleaded for the elimination of antitrust intervention.

The Chicago School analysis on antitrust has deeply influenced the principles as well as the instruments of antitrust intervention. Consumer welfare has been recognised as the main goal of antitrust, and economic analysis has increased its role in the lawyers' and Courts' approach to antitrust cases. Nevertheless, ideological debates on the soundness of antitrust have been substituted by debates focused on the technical issues, in part due to the renovated trend of business concentration.

2.3. THE PROCESS OF DEREGULATION.

21. The Chicago School. In the 1960s, the group of scholars of the University of Chicago extended the scope of their research method from antitrust to other kinds of public intervention, particularly to regulation by independent agencies. In their articles in *The Journal of Law and Economics,* Coase,[57] Stingler, Posner, Demsetz and other academics, challenged the common wisdom and affirmed that public intervention was often inefficient, and that it had a tendency to defend not the general interest but the interest of powerful groups, particularly the interest of the regulated industry.

Firstly, price fixing by the regulatory authorities was accused of being inefficient. This kind of intervention obstructed the definition of prices by regular market mechanisms, and at the same time was incapable of imposing an effective control on the regulated industry due, amongst other factors, to the

[57] One of the seminal articles was COASE, R. (1960): "The Problem of Social Cost", in *The Journal of Law & Economics*, vol. 3, p. 1-44.

asymmetric distribution of information in favour of the industry.[58] According to the traditional normative theory, price regulation by the regulatory commission was supposed to limit the benefits of the regulated industry to a "fair return" of the capital invested. In practice, this mechanism on the one hand protected the industry, since the fair return was ensured by tariffs increases even in those cases where cost increases would be caused by inefficient management. On the other hand, the price fixing mechanism did not impose an effective control.[59] It has been demonstrated that an overcapitalisation (an investment ahead of demand), would ensure an automatic increase of the "fair return" (Averch-Johnson effect).[60]

Furthermore, the regulatory intervention was accused of favouring private interests, rather than the general interest as traditionally considered.[61] The new study approach assumed that the relationship between the regulatory authorities and the regulated industry would not be free of the rational pressures emanating from industry to use public intervention for the fulfilment of their desires. The analysis of different regulatory authorities[62] proved that even if originally created to pursue general interest objectives, the authorities often were "captured" by the regulated industry, and often they became "a device for

[58] BAUMOL, W. (1970): "Reasonable Rules for Rate Regulation", in *"The Crisis of the Regulatory Commissions"*, J. Wilson, Basic Books, New York, p. 188.

[59] This was the case for example of the regulatory intervention in the power sector, see STIGLER, G. and FRIEDLAND, C. (1971): "What Can Regulators Regulate? The Case of Electricity", in *The Journal of Law & Economics*, vol. 5, p. 11.

[60] As was said by Stigler in his seminal article "price control is essential to achieve more than competitive rates of return", STIGLER, G. (1971): "The Theory of Economic Regulation", in *Bell Journal of Economics and Management Science*, vol. 2, no. 1, p. 6.

[61] "As a rule, regulation is acquired by the industry and is designed and operated primarily for its benefits", *ibid.* STIGLER (1971), p. 3.

[62] The studies included the FCC: COASE, R. (1959): "The Federal Communications Commission", in *The Journal of Law & Economics*, vol. 2, pp. 1-40.

transferring income to well-organised groups if the groups will return the favour with votes and contributions to politicians".[63]

As it will be shown[64], for decades, the FCC confirmed the analysis of the Chicago School according to which "every industry that has enough political power to utilise the State will seek to control entry. In addition, the regulatory policy will often be so fashioned as to retard the rate of growth of new firms".[65]

22. Alliance of interest against public intervention. After decades of economic prosperity after World War II, economic growth in the US had stabilised by the end of the 1960s, and had given place in the 1970s to an economic crisis, with very low growth and high inflation.

The economic situation of the regulated industry was threatened for the first time since the introduction of the regulatory intervention. The participation of consumers and citizens in the activity of the regulatory commissions[66] obstructed the tariff modifications necessary to adjust tariffs to the rising costs brought about by inflation. As a result, the benefits of the regulated industry declined (phenomenon which is referred to as "regulatory lag"). The regulated industry adopted a negative approach against the regulatory intervention that had traditionally benefited the industry. The regulated industry, making use of the intellectual arguments developed by the Chicago School in the precedent decade, connected the economic crisis to the excessive intervention of the public authorities in the economy, and initiated a debate on the role of public authorities in economic activity.

In parallel, price regulation had often created cross-subsidies between different services of the same sector. After decades of such a policy, important

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[63] JOSCOW, P. and NOLL, R. (1981): "Regulation in Theory and Practice: an Overview", in "*Studies in Public Regulation*", G. Fromm, MIT Press, New York.

[64] *Vide infra* 2.4.2. The Regulated Monopoly (1921-1969).

[65] *Vide* STIGLER (1971), p. 5 (*supra* footnote 60).

[66] *Vide supra* Chapter 2.1. Origins and Evolution of Economic Regulation.

divergences between costs and tariffs emerged, and as a direct result, certain categories of consumers were forced to finance services for other categories. When the criticism of regulation reached a certain volume, these groups joined the anti-regulatory party and tried to eliminate regulation.

The early criticism of public intervention initiated by the Chicago School not only influenced the regulated industry, it also influenced politicians in search for policies to fight the economic crisis. The reduction of inefficient public intervention became the main proposal of the conservative sectors led by Ronald Reagan, for the superation of the economic crisis. In this way, an alliance between conservative politicians, the regulated industry, and certain groups of consumers, with the intellectual arguments of the Chicago School, forced the deregulation of the American economic activity.

23. Deregulation. Deregulation does not necessarily mean elimination of the regulatory intervention. Rather, it means a relaxation of the obligations imposed on the private operators by the regulatory agencies for the fulfilment of the general interest. Deregulation affected all kinds of public intervention, from social regulation, to antitrust, but the most affected was the price-and-entry regulation.

Conservative administrations such as the Reagan's one, reduced the budget of most of the regulatory commissions, obstructed their decision-making process, and imposed a cost-benefit analyses of all the regulatory measures. The effect on social regulation was a relaxation of the obligations imposed on the industry, but not an elimination of this kind of intervention, nor a structural modification of the intervention instruments.

The effects on price-and-entry regulation were more profound. The regulatory agencies created during the New Deal substituted the free market mechanisms by rate regulation and the limitation of market entry through restrictions in license granting. The regulatory reform did not eliminate the

regulatory agencies nor significantly modified their procedures or the nature of the intervention instruments, but it did deeply modify the principles of regulatory intervention. Restrictions to market entry were eliminated and rate regulation questioned. Market substitutive intervention gave place to a market complementative intervention, in which demand and supply mechanisms in a market without entry restrictions would rule private activity in the sector, with a mere subsidiary intervention to solve certain market failures.

The new regulatory approach is not necessarily simpler. As a matter of fact, market complementative regulation, and particularly the introduction of schemes for the promotion of competition, has probably increased the complexity of public intervention. This seems almost necessary, since the tendency towards conflict in a market with an unlimited number of economic operators in competition with a former monopolist with significant market power is bigger than in a market were only three main forces: the monopolist, the regulator and the consumers, interact.

Even if the institutional framework and the basic nature of the regulatory intervention as an indirect intervention are maintained, the deregulation process has substantially modified the principles and the instruments of public intervention by regulatory agencies in general interest sectors. This reform has to be taken into account in any attempt to adopt the regulatory model in the European Union.

2.4. PUBLIC INTERVENTION IN THE US TELECOMMUNICATIONS SECTOR.

2.4.1. Origins and Free Competition in the US Telecoms Markets (1876-1921).

24. Patent monopoly in the telephone market (1876-1894). On February 17, 1876, two patent requests were filed, claiming the benefits for the

invention of the telephone. Alexander Graham Bell filed his patent request two hours before Elisha Gray. This was the origin of a dispute, which took place mainly in Court, and ended with the final recognition of Bell's patent and the exit of the market by the competitor.[67] As a result, until 1894 the Bell Telephone Company enjoyed an exclusivity for the exploitation of the invention.[68]

Once Bell's monopoly was firmly established, the growth in the development of the network was reduced due to the high tariffs, the poor quality of the service, and the focus of the company in the major commercial centres of the country, with very little attention to small towns and rural areas.[69] The Bell Telephone Company adopted a new structure. AT&T was created to be the head of the Bell System, to define its strategies and provide the long distance service. Horizontally, the System was formed by regional operators providers of local telephony services, financed by local capitalists that would give an important share (from 35% to 50%) of the companies to AT&T for the granting of the license to operate. Vertically, the Bell System was integrated by the Bell Telephone Laboratories, that would become the leading R&D centre of the world, and Western Electric, in charge of manufacturing terminal and switching equipment.

25.-Full competition in the telephone market (1894-1907). When the main patents expired, thousands of newcomers entered the market.[70] The first

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[67] For the dispute *vide* STONE (1991), pp. 54-62 (*supra* footnote 9).

[68] As stated by the President of the company in 1880 "with a through occupation of the principal cities and towns by our licensees, the ownership of the broad patents covering the use of the speaking telephone, and the control of nearly all the inventions for the apparatus necessary to the telephone business which have yet been made, the danger of competition with our business from new comers seems small", AMERICAN BELL TELEPHONE COMPANY (1880), Annual Report.

[69] See TOSIELLO, R. (1979): "*The Birth and Early Years of the Bell Telephone System, 1876-1880*", Arno Press, New York.

[70] By 1902 there were over 9,000 "independent providers", of which around 3,000 were commercial providers, 1,000 mutualistic companies, and 5,000 providers of services to a few dozens of grangers, FISHER, C. (1987): "The Revolution in Rural Telephony", in *Journal of Social History*, vol. 21, p. 6.

stage involved the new comers offering their services in areas not covered by the Bell System, but as early as 1895 they started to run exchanges in towns served by the Bell System.[71] The Bell System initially obstructed the entrance of new comers through patent litigation based on the hundreds of minor patents controlled by the System, even if the main patents had already expired, while high prices and poor service were maintained.[72]

The strategy was modified when the "independents" started to compete directly with Bell's exchanges. At that point, the prices of the Bell System were reduced (even if only in those exchanges were direct competition was suffered), sometimes maybe under cost,[73] even if, in general, they were maintained at a higher level than the "independent's" prices and did not enter in price wars. In parallel, the Bell System initiated a strategy of development of their networks ahead of demand, in order to avoid the competitors' dominance in those areas.[74]

Furthermore, the Bell System implemented a strategy to obstruct the development of the new comers. Interconnection was refused, in such a way that the new comers' clients could not connect with the long distance network of AT&T, nor communicate with the Bell System's clients in their towns. At the same time, Western Union refused to sell equipment to the new comers. Furthermore, the three main cities of the country, New York, Chicago and

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[71] See WIENHAUS, C. and OETTINGER, A. (1988): "*Behind the Telephone Debates*", Ablex Publishing, Norwwod NJ, pp. 7-8.

[72] See NIX, J. and GABEL, D. (1993): "AT&T's Strategic Response to Competition: Why not Pre-empt Entry?", in *The Journal of Economic History*, vol. 53, no. 2, pp. 377-387.

[73] See WEIMAN, D. and LEVIN, R. (1994): "Preying for Monopoly? The Case of Southern Bell Telephone Company, 1894-1912", in *Journal of Political Economy*, vol. 102, no. 1, pp. 110-114.

[74] According to a Southern Bell representative "We have scraped along for the past ten years, building exchanges and toll lines that we ought not have constructed except for the purpose of causing the service to be more valuable than that of our adversary", in *Telephony*, January 30 1909, in MUELLER, M. (1993): "Universal Service in Telephone History", in *Telecommunications Policy*, vol. 17, no. 5, p. 360.

Boston, refused to grant licenses for the construction of new telephone networks, maintaining the monopoly of the Bell System.

The result of the fierce competition was a significant reduction of prices, both of the services and of the terminal equipment,[75] an impressive expansion of the services,[76] particularly in rural areas,[77] and the loss by the Bell System of half of the market share by 1907.[78] The Bell System's refusal to allow interconnection created uncomfortable situations, since some users were forced to contract with more than one company in order to reach all the telephone users in their towns.

26. Monopolisation by the Bell System (1907-1921). Price reduction and development of the network ahead of demand, forced the Bell System to accept the control by a new capitalist, J.P. Morgan, who imposed in 1907 the return to the Presidency of AT&T of Theodore Vail and a change in the strategy of the company. The new strategy was to eliminate competition from the telephony market.

The first element of the new strategy was the acquisition of competitors.[79] This measure allowed the Bell System to develop its network without building,

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[75] See GABEL, R. (1969): "The Early Competitive Era in Telephone Communication, 1893-1920", in *Law and Contemporary Problems*, spring, pp. 343-346.

[76] From 270,000 lines in 1894 to 6,100,000 lines in 1907, See FEDERAL COMMUNICATIONS COMMISSION (1939): "*Investigation of the Telephone Industry in the United States*", US Government Printing Office, Washington DC, p. 151.

[77] In 1912 38% of the telephone lines were installed in rural areas, and in 1920, the telephone penetration rate was higher in rural areas, 39%, than in urban areas, 35%, *vide* FISHER (1987), p. 8 (*supra* footnote 70).

[78] See LIBOIS, L. (1983): "*Genèse et croissance des telecommunications*", Masson, Paris, p. 317.

[79] "Most Independents still felt very intensely over what they described as the 'Bell taint' and bitterly fought purchases of Independent properties and Bell wire connections. This, of course, did not deter the Bell people from buying any plant they desired and could get. And they picked up a good many of them, due to different reasons. Sometimes the owners had failed to make the profits they had believed were in the business; sometimes they were offered such a handsome bonus on their investment that they could not resist; in other cases, cut rate warfare exhausted their resources and forced a sale", see MACMEAL, H. (1934): "*The Story of Independent Telephony*", Independent Pioner Telephone Association, Chicago, p. 172.

and at the same time to eliminate competition from the market.[80] The Bell System not only acquired competitors in the telephony market, but it also acquired potential competitors like the telegraph monopoly, Western Union, in 1913.

A second element of the new strategy was to ensure a monopoly on the long distance network.[81] AT&T started to negotiate exclusive interconnection agreements with some of the "independents" in order to avoid the creation of an alternative long distance network. The acquisition of Western Union had the same objective. Furthermore, the Bell System actively obstructed any attempt to create an alternative network. In 1901, a new competitor managed to control 11% of the lines in the US. In order to develop the network it needed major financial support. Although it was provided by the American Ice Company, at the end of the day, the American Ice Company turned out to be working for the Bell System, which ensured the failure of the project.[82] This was not the only occasion in which the Bell System intervened to ensure its monopolistic position in the long distance market.[83]

The ultimate strategy for the monopolisation of the telephony market by the Bell System was the introduction of regulation. Firstly, the Bell System considered that regulation at a State or federal level could be more easily "captured" than at the local government level where obligations were already

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[80] Acquisitions not only eliminated competition from the operator acquired, but also from neighbouring operators which could not connect anymore with these networks and remained therefore isolated.

[81] "I take it that it is extremely important that we should control the whole toll line system of intercommunication throughout the country. This system is destined, in my opinion, to be very much more important in the future that it was in the past. Such lines may be regarded as the nerves of our whole system. We need no fear the opposition in a single place provided we control the means of communication with other places". Letter from G. Leverett, of the legal staff of AT&T, to F. Fish, president of AT&T, in 1902, in LANGDALE, J. (1978): "The Growth of Long-distance Telephony in the Bell System: 1875-1907, in *Journal of Historical Geography*, vol.4, no. 2, p. 148.

[82] See BROCK, G. (1981): "*The Telecommunications Industry. The Dynamics of Market Structure*", Harvard University Press, Cambridge, MA, pp. 119-120.

[83] J.P. Morgan forced some bankers to retire from an operation financing the creation of a long distance competitor, *vide* GABEL (1969), p. 350 (*supra* footnote 75).

being imposed on the telecommunications operators. This was the experience with the State regulatory authorities and with the Interstate Commerce Commission.[84]

The Bell System initiated a campaign promoting public intervention in the market to ensure the integration of the market, that is, the creation of a single interconnected network. Since the Bell System refused to interconnect their network with the independent networks,[85] the only way to ensure the unification of the service was the elimination of competition and the creation of a monopoly under the control of the public authorities.[86]

At the same time, the important market share of the Bell System,[87] and the acquisition of competitors policy, risked provoking the intervention of the antitrust authorities. The Bell System considered that the institution of another type of public intervention in the market, like regulation by independent agencies, would prevent the application of the rules on antitrust, as it was the case for example in 1913, when the Attorney General asked for the intervention

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[84] The Mann-Elkins Act, June 18, 1910, expanded the competencies of the Intersate Commerce Commission to the telecommunications sector. Nevertheless, the ICC, only undertook four minor actions in the sector, always acting on the basis of complaints, *vide* GABEL (1969), pp. 537-538 (*supra* footnote 75).

[85] Mr. Vail sustained that compulsory interconnection would be a legally approved confiscation of property, AT&T (1910), Annual Report, pp. 44-46.

[86] The Bell System's strategy was openly defined in its Annual Reports: "It is not believed that this [integration of the service] can be accomplished by separately controlled or distinct systems nor that there can be competition in the accepted sense of competition. It is believed that all this can be achieved to a reasonable satisfaction of the public with its acquiescence, under such control and regulation as will afford the public much better service at less cost than any competition or government-owned monopoly could permanently afford." AT&T (1910) Annual Report, p. 23. "It is contended that if there is to be no competition, there should be public control. It is not believed that there is any serious objection to such control, provided it is independent, intelligent, considerate, thorough and just, recognising, as does the Interstate Commerce Commission", AT&T (1907) Annual Report, p. 18. "This "supervision" should stop at "control" and "regulation" and not "manage", "operate" nor dictate what the management or operation should be [...] here is to be state control and regulation, there should also be state protection, protection to a corporation striving to serve the whole community [...] from aggressive competition which covers only that part which is profitable". AT&T (1910) Annual Report, p. 32-33.

[87] The market share of the Bell Sytem in 1912 was 59%, and reached 79% taking into account the exclusive agreements with some of the independents, *vide* GABEL (1969), p. 352 (*supra* footnote 75), and STONE (1991), p. 188 (*supra* footnote 9).

of the Interstate Commerce Commission, instead of the initiation of an antitrust procedure, for the acquisition of certain "independents" in Chicago.

2.4.2. The Regulated Monopoly (1921-1969).

27. General. The Bell System strategy to promote regulatory intervention in order to facilitate the monopolisation of the telecommunications sector reached its success in 1921 when the Willis-Graham Act was adopted. This legislation allowed telephone operators to acquire any competitor with only the approval of the ICC and the exclusion of the antitrust authorities. This meant the acceptance of the principle that regulation was a sufficient control of the market, even in such a concentrated market as telephony.

In 1934 the Federal Communications Commission (FCC) was created, merging the regulatory activities in the telecommunications and radio/television sectors. The new authority, with the powers granted by the 1934 Telecommunications Act, enforced the entry-and-price regulation model common in the New Deal period. The first action of the new commission was to launch a deep investigation of the sector.[88] The most important lines of action of the FCC in the telecommunications sector were, firstly, the conscious imposition of limitations to market entry through restrictions in the granting of licenses, and secondly, the development of a cross-subsidy scheme in order to reduce the cost of the local communications and increase the tariffs of the long distance communications.

28. The creation of conditions for deregulation. The quarter of a century that followed the creation of the FCC allowed the full implementation of the entry-and-price regulatory model in the telecommunications sector. There were two important features of the regulatory model in the telecommunications sector which favoured the future deregulation of the

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[88] Federal Communications Commission (1939): "*Investigation of the Telephone Industry in the United States*", US Government Printing Office, Washington DC.

sector, as they created groups of actors interested in the reform of the sector: Firstly, the Consent Decree of 1956, which restricted AT&T's activities to the hard-core of telecommunications, and secondly, the separation procedures, which provoked an increasing divergence between costs and prices,.

29. The 1956 Consent Decree. The investigation of the telecommunications markets launched by the FCC after its creation, already showed some signs of abusive behaviour by the Bell System in relation to prices of telecommunications equipment.[89] However, due to the eruption of World War II, and the important role of the Bell System, and particularly its manufacturing division Western Electric, in the conflict, no immediate action was undertaken.

Once the war was over, in 1949, the Justice Department filed a complaint requiring the court to divest Western Electric from the Bell System. The conservative Administration of Eisenhower terminated the suit with a 1956 Consent Decree. It did not force divestiture, but forced Western Electric to license its patents and to manufacture telephony equipment exclusively, and forced the Bell System to provide only the kind of services subject to regulatory control by the FCC.[90]

At that time, the 1956 Consent Decree was considered a victory for the Bell System, since the limitations to operate exclusively in the regulated telecommunications market did not seem particularly restrictive, especially in a period of impressive growth of the telecommunications market.[91]

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[89] The Report stated that Western Electric's prices bear no reasonable relation to the cost of manufacture, and has an appreciable influence on the cost of the telephone service, Federal Communications Commission (1939): "*Investigation of the Telephone Industry in the United States*", US Government Printing Office, Washington DC, pp. 579-589.

[90] *US v. Western Electric Co.*, CA No. 17-49, Final judgement, 1956 Trade cas. (D.N.J. 1956).

[91] See TEMIN, P. (1987): "*The Fall of the Bell System. A Study in Prices and Politics*", Cambridge University Press, New York, p. 15.

30. Cross-subsidiarisation. The second important feature was the implementation of the separations policy. Market structure and the vertical distribution of political power in the US, provoked a conflict over whether local loop costs should be borne exclusively by the local operator or partially allocated to the long-distance operator.[92] The *Smith v. Illinois Bell Telephone Company* judgement put an end to this a conflict. In its ruling it stated that "it is obvious that, unless an apportionment is made, the intrastate service to which the exchange property is allocated will bear an undue burden - to what extent is a matter of controversy".[93]

The controversy on the extent of the allocation of costs to the long-distance operator was solved in 1943 with the approval of the *Separations Manual*, by a joint board of federal and State regulators. The *Separation Manual* initially fixed that the proportion of costs allocated to long-distance operators would be the same as the proportion of minutes of usage of the local-loop for long distance communications (at that moment 3%)[94]. The Bell System accepted such compromise, which mostly provoked a minor internal cost accounting modification, since they controlled most of the long-distance and local-loop facilities. Over time, the percentage of costs allocated to the long-distance operator increased,[95] and as a result, divergence between costs and

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[92] Two different conceptions on the allocation of the local loop costs were in conflict. According to the board-to-board conception, local loop costs (the costs of the "last mile") should be borne by local operators and ruled by state regulatory commissions, while according to the station-to-station conception, a portion of the local loop costs should be attributed to the long-distance operator, since long-distance communications took profit of the "last mile" to initiate and terminate communications, and in parallel, the FCC should intervene in the regulation of such costs.

[93] *Smith v. Illinois Bell Telephone Co.*, 282 U.S. 1930.

[94] See CRANDALL, R. (1991): "*After the Break Up. U.S. Telecommunications in a More Competitive Era*", The Brookings Institutions, Washington D.C., p. 24.

[95] As the usage of long-distance increased, the percentage of costs allocated to long-distance also increased. Nevertheless, the increase was substantially higher due to the tendency of the State Regulatory Commissions (allied in the National Association of Regulatory Utility Commission, NARUC) to lower local tariffs through the allocation of costs to long-distance operators. This tendency was favoured by the reduction of long-distance communications (due to technologic progress) and by the fact that the tendency increased the Bell System benefits since the FCC rates of return were usually higher than the state regulators. According to WYNNS, P. (1984): "*The Changing Telephone Industry: Access Charges, Universal Service and Local Rates*", Congressional Budget Office, Washington D.C,

prices increased. This divergence was reinforced by the policy of uniform geographic rates, cross-subsidiarisation from urban to rural areas, and from business to residential users.

31. First measures of reform. The first fissure in the regulated monopoly system appeared when large telecommunications users for example TV stations, disadvantaged by cross-subsidies from long-distance to local telephony, required licenses from the FCC for the establishment of private communications systems with point-to-point microwave links. Small manufacturers (such as Motorola) were also interested in the apparition of alternative clients to the Bell System, supplied by its subsidiary Western Electric. The FCC in its *Above 890* decision, opted for the allocation of frequencies to such users.[96] AT&T launched a new tariff scheme with large discounts, called Telpak, that tried to eliminate the incentive for the construction of private systems. The possible predatory and anticompetitive character of AT&T's response to the establishment of private communications systems forced public intervention[97] and created distrust for the regulated monopolist.

Different decisions affected also the Bell System's position in the terminal equipment markets. In 1956 a Court of Appeal rejected a FCC decision that approved the Bell System refusal to allow the attachment to the telephone of a plastic mechanical device that enabled more private conversations (*Hush-A-Phone*).[98] This precedent probably put pressure on the FCC to rule against the Bell System on a similar case related to a more

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p. 10, by 1984 the percentage of costs allocated to long-distance was around 27%, while the percentage of long-distance usage was around 8%.

[96] FCC, *Report and Order*, FCC Docket 11866, "Above 890 Mc.", July 1959, 27 FCC 359.

[97] Motorola filed a complaint before the FCC. After fifteen years of proceedings, the FCC considered that Telpak tariffs were contrary to the 1934 Telecommunications Act because they were discriminatory, predatory and therefore illegal, see BROCK, G. (1981): "*The Telecommunications Industry. The dynamics of Market Structure*", Harvard University Press, Cambridge, MA, pp. 208-210.

important electric device to provide mobile links with the fixed network, the *Carterfone*, in such a way as to enable users to provide their own terminal equipment, as long as it would not harm the network.[99]

2.4.3. Deregulation of the US Telecom Markets (1969-2000).

32. The reform of the US telecom markets. It can be argued that the origin of the deregulation of the telecommunications markets has been the very same success of the entry-and-prices regulatory model imposed by the 1934 Telecommunications Act. On the one hand, such a regulatory model forced the monopolist to concentrate its activities in the hard core of the telephony activity.[100] If initially this restriction did not seem to impose a real constraint on the monopolist, in the long term it produced decisive pressure from companies grown in competitive neighbouring markets to open also the telecommunications markets to competition. On the other hand, the success of the entry-and-price regulation allowed the development of a market structure characterised by the existence of important cross-subsidies and other unbalanced situations, which provided arguments and support for the gradual opening of the markets to new operators.

Its complexity, long duration, the initial lack of a clear alternative model, and the limited influence of foreign models has characterised the process of reform of the US telecommunications markets. From 1934 to 1969 the conditions that would later facilitate the transformations had developed up to a certain degree due to of pressure from the antitrust authorities. As a result, limited reforms were introduced, more with the aim of providing solutions to

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[98] *Hush-A-Phone Corp. v. United States*, 238 F. 2d 266 (D.C. Cir.) 1956.

[99] In the matter of Use of the Carterfone Device in Message Toll Telephone Service, 13 FCC 2d 420 (1968), see HORWITZ, R. (1989): "*The Irony of Regulatory Reform. The Deregulation of American Telecommunications*", Oxford university Press, New York, pp. 230-231.

[100] This was necessary in order to avoid conflicts with the antitrust authorities. Furthermore, the monopolist had to devote all its resources to match the extraordinary growth of the demand for the telephony service.

specific conflicts than of reforming the sector according to a conscious plan. Such measures, nevertheless, created new markets and led to a first period of reforms, from 1969 to 1996. At this point, the dominant conservative positions in favour of deregulation, together with pressure from the new actors in the sector and from the groups damaged by the regulatory unbalances, forced a major reform, this time aimed at eliminating traditional regulation for significant market segments, and at forcing the monopolist to divestiture in order to create a new market structure compatible with competition.

The last period of the process of reform, from 1996 onwards, extended the reform to these segments previously exempted- mainly the local telephony markets- and implemented the full deregulation of the telecommunications markets.

33. The first deregulation wave (1969-1996). By the end of the 1960s and the beginning of the 1970s new management had control over the Common Carrier Bureau of the FCC. The influence of the Chicago School doctrines and the conservative political positions on deregulation, as well as pressures from large telecommunications users and companies trying to access the telecommunications markets, led to the adoption of a conscious strategy to deregulate the market, to eliminate the most invasive entry-and-rate regulation and to open significant segments of the telecommunications markets to competition. The abusive behaviour of AT&T in response to the introduction of competition led to an antitrust procedure that finished with the divestiture of the Bell System in 1984.

34. Competition in telecommunications services. In 1969, the FCC, in a 4 to 3 vote, approved an application by MCI, a small under-financed company, to build a microwave system between Chicago and Saint Louis. The decision was the beginning of the end of the entry-and-price regulation, since the application was not for a private system, as in the *Above 890* decision, but for

system providing long-distance services to the public in competition with AT&T. In response to the flow of applications, the FCC published the *Specialized Common Carriers* decision,[101] which accepted the introduction of competition in specialised services,[102] despite the allegations and lobbying of the Common Carriers.[103] In 1975 MCI initiated the provision of a new service, Execunet, which substantially competed with the common long-distance activities of AT&T. The FCC ordered MCI to eliminate such a non licensed service, however the Court of Appeals reversed this order,[104] thus allowing MCI and the rest of specialised carriers to compete in all the long-distance telecommunications markets.[105] During the 1970's other value-added services were opened to competition.

35. AT&T's divestiture. A new antitrust suit[106] against the attempts to monopolise the telecommunications markets was launched by the Justice Department in 1974. The Bell System was accused of conspiring to monopolise various telecommunications markets. Initially the suit was focused on the anticompetitive effects of the vertical integration of the System, and the

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[101] "Competitive pressure may encourage beneficial changes in AT&T's services and charges in the specialised field and stimulate counter innovation or the more rapid introduction of new technology", In the Matter of Establishment of Policies and Procedures for Consideration of Applications to Provide Specialised Common Carrier Services in the Domestic Public Point-to-Point Microwave Radio Service and Proposed Amendments to parts 21, 43, and 61 of the Commission's Rules, 29 FCC 2d 870 (1971).

[102] This kind of communications were increasingly important, since they match the demand of reliable communications by the computer industry. The convergence between computers and telecommunications forced the FCC to determine rules identifying the border line between telecommunications regulated activities and non-regulated computer activities, particularly important, since the 1956 Consent Decree restricted the Bell System activities to the telecommunications sector.

[103] Common carrier argued that such licenses would take profit of the cross-subsidiarization for the development of universal service, 'screaming' the market. On this issue, see BROCK, W. and EVANS, D. (1983): "Cream-skimming", in "*Breaking Up Bell. Essays on Industrial Organization and Regulation*", North-Holland, New York, pp. 61-94.

[104] "The ultimate test of industry structure in the communications common carrier field must be the public interest, not the private financial interest of those who have until now enjoyed the fruits of *de facto* monopoly", MCI Telecommunications Corp. v. FCC, 561 F. 2d 356 (D.C. Cir 1977), p. 380.

[105] See CURIEN, N. and GENSOLLEN, M. (1992): "*Economie des télécommunications*", Economica, Paris, pp. 170-171.

[106] See the important role of antitrust in the deregulation of the telecommunications industry in BAKER, D. and BEVERLY, B. (1983): "Antitrust and Communications Deregulation", in *The Antitrust Bulletin*, vol. 28, pp. 1-38.

abusive behaviour of Western Electric. It proceed quite slowly. In a second stage, the anticompetitive response of the Bell System to competition in the long-distance communications markets accelerated the procedure.

After the *Execunet* decision the Bell System had two main strategies. On the one hand, AT&T significantly reduced its private lines rates in the high density lines, (Hi-Lo scheme), in order to face competition from new comers.[107] This brought about accusations of predatory pricing from competitors. On the other hand, the local monopolist, vertically integrated in the Bell System, firstly refused interconnection for the provision of the *Execunet* service, and when the Court of Appeals mandated to provide such interconnection, the Bell System filed a tariff scheme, ENFIA, which intended to impose specialised carriers charges equal to those required to AT&T for local interconnection, in order to avoid the "screaming" of the market.[108]

Pressure from the long antitrust process (which menaced to enforce the divestiture of Western Electric), and from the new political conservative Presidency (in favour of deregulation and competition), forced the Bell System to reach an agreement with the Justice Department. On January 8, 1982 the settlement of the case was announced. The vertical integration between AT&T (the long-distance provider), Western Electric (the manufacturer), and the Bell Laboratories (the R+D subsidiary) was respected, and such a group would be released from the restrictions defined in the 1956 Consent Decree. The price to pay by the Bell System was to renounce to the horizontal integration with the local operating companies, which would form seven different companies,

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[107] In this way, an exception to the traditional principle of national averaging was introduced, see TEMIN, P. (1987): "*The Fall of the Bell System. A Study in Prices and Politics*", Cambridge University Press, New York, p. 77.

[108] An agreement was reached to reduce such charges, but only temporary.

subject to the traditional entry-and-price regulation. Judge Green finally accepted the agreement on August 24.[109]

The agreement entered into force in 1984. The country was divided into 163 Local Access and Transport Areas (LATA), intra-LATA services would be exclusively provided by Local Exchange Carriers (mostly by the seven Baby Bells, but also by some independent companies still present in the market) under entry-and-price regulation. Inter-LATA and international services would be provided by Interexchange Carriers (AT&T, MCI and others) under competition. Interexchange carriers could not provide intra-LATA services, while the Baby Bells could not provide inter-LATA services nor manufacture equipment. In order to make the new framework sustainable, the principle of equal access to the Baby Bells' local networks (Open Network Architecture and Comparable Efficient Interconnection) was enforced, and access charges for the termination of inter-LATA and international communications were established.

36. The second deregulation wave (1996-1999). On February 1998, President Clinton signed the 1996 Telecommunications Act, which extended deregulation also to the local markets. The entry-and-price regulation maintained in the local markets was eliminated. Interexchange carriers and any other operator would be able to establish networks and provide local services. At the same time, the elimination of the restrictions imposed by the 1982 Modified Final Judgement on the Baby Bells was foreseen. The Baby Bells would be able to manufacture equipment, and more important, would be able to provide inter-LATA services. The Baby Bells would be able to provide inter-LATA service outside their regions from the first moment, but for the provision of such services in the regions where they had enjoyed exclusivity, entrance to the long-distance market was connected to the evolution of competition in the

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[109] *US v. AT&T*, CA No. 82-0192 (D.D.C.), Modification of Final Judgement, August 24, 1982, *vide*

local-loop, in such a way that authorisations would only be granted by the FCC if a series of conditions proving the existence of competition were met.[110]

2.5. CONCLUSIONS.

37. Final. It has been shown that both antitrust and sector specific regulation by independent agencies appeared at the same time and as a political response to the pressures imposed by the economic structures generated by industrialisation in the 19th century.

Whilst in Europe the most relevant of the new economic activities were monopolised by public authorities, in the US such activities were undertaken by private entities. Nevertheless, the first mover advantage, the economies of scale of the network industries and the strategy of many of the entities led to the monopolisation of the markets by private entities.

Both antitrust and sector specific economic regulation appeared as public intervention mechanisms of an indirect nature. Their scope was to control the economic power of private entities for the common benefit. Nevertheless, the evolution of both instruments of public intervention during the 20th century is prove of the risks of over-regulation.

Antitrust, due to the lack of economic analysis, became an obstacle to economic efficiency and consumer welfare. Sector specific regulation often became a mechanism for the protection of the interests of the regulated industry.

TEMIN (1987), Chapter VII (*supra* footnote 107).

[110] See KRATTENMAKER, T. (1996): "The Telecommunications Act of 1996", in *Federal Communications Law Journal*, vol. 29, p. 1; SCHWARTZ, M. (1999): "Conditioning the Bell's Entry into Long Distance: Anticompetitive Regulation or Promoting Competition?", in *"The anticompetitive Impact of Regulation"*.

The deregulatory movement has managed to replace the market substitutive intervention by a market complementative intervention. Free market mechanisms are not to be negleted but merely complemented in those cases in which a cost-benefit analysis proves that a market failure exists.

This evolution does not require a structural reform of the institutional regulatory framework, nor the introduction of new regulatory instruments. On the contrary, the long-lasting regulatory tradition only requires adjustments with regard to the objectives of such intervention. Competition in the market is to be protected and complemented, but not substituted.

CHAPTER 3

NATIONALISATION AND LIBERALISATION OF THE EUROPEAN TELECOMS MARKETS

SUMMARY: 3.1. Evolution and the nature of public intervention in Europe. 3.2. Competition Law in Europe. 3.3. The process of liberalisation. 3.4. Public intervention in European telecommunications. 3.5. Conclusions.

3.1. EVOLUTION AND THE NATURE OF PUBLIC INTERVENTION IN EUROPE.

3.1.1. Precedents of the *service public* model.

38. Early precedents. The earliest precedents of the *service public* model in Europe are to be found in structures that developed at the end of the Middle Ages. Certain structures and institutions that appeared in the feudal rural areas,

and mainly in towns, influenced by the *utilitas publica* doctrine, drew some of the characters of the future notion of *service public.*[111]

In the feudal countryside certain structures appeared that had some characteristics in common with today's *service public* notion. The *banalités seigneuriales*, such as mills or bridges, were provided by the Lord to his vassals, who had the obligation to use and pay for them as long as the Lord could ensure the continued and equal provision of the service. If the Lord could not provide the service under such conditions, vassals had the right to obtain the service from a different provider. Continuity and equality in the provision are two of the main characteristics of the *service public* notion.

Urban development by the end of the Middle Ages led to the appearance of activities which were of common interest for the neighbours of the town. Activities such as the maintenance of the walls, the cleaning of the streets or the organisation of the market, were services of general interest provided by the local government. Services such as the butcher's or schooling were also provided by the local government under an exclusive right.[112] The provision of these services required a special legal regime, distinct from civil law.

Both precedents of the *service public* notion were affected by the doctrine of the *utilitas publica*, received from Roman Law by the 13th century. The rescued doctrine legitimised the supremacy of the general interest over the private interest.

39. Absolute monarchies. Direct precedents of the *service public* notion only appeared with the strengthening of the monarch's power. It is for this

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[111] This section follows the historical research of JOURDAN, P. (1987): "La formation du concept de service public", in *Revue du Droit Public et de la Science Politique en France et a l'Étranger*, pp. 89-118; MESCHERIAKOFF, A. S. (1991): "*Droit des services publics*", Presses Universitaires de France, Paris, preliminary chapter; and the brilliant book by MESTRE, J. L. (1985): "*Introduction historique au droit administratif française*", PUF, Paris.

[112] *Ibid.* MESTRE (1985).

reason that the concept of *service public* is particularly strong in those European countries where absolute monarchies and a strong centralised power developed (or in those countries where this philosophy had a strong influence, such as Belgium and Italy).

The postal system in France is a highly interesting example. In 1464 King Louis XI decided to create a postal service for the improvement of the efficiency of the new administration of the kingdom. The postal service was used to connect the administrators all around the country. It was, then, a service created by the King to improve his administration. Only in exceptional cases was the service opened to private use by the general public. It was only in the 17th century, due to the success of the service, and the need of revenues for the Crown, that the postal monopoly was declared open to the public.

Together with the post, the Crown provided other services. By the eighteenth century there was a set of what was known in France as "*services du public*". These services had three main characteristics. Firstly, they were provided by the public authority (the Crown). Secondly, they were offered to the general public, and not to a particular category. Thirdly, they were not ruled by Private Law, but by Public Law. These services, (post, bridges etc.) had as their main goal getting revenues for the Crown by charging the public for the provision of a service of general interest.

A parallel development during the age of absolute monarchies, was the expansion of local monopolies for the provision of services of general interest. A good example is the creation by the local government of Marignane (France), in 1655, of a communal baker with a monopoly right, in order to ensure the continued provision of bread at a reasonable price.[113]

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[113] *Vide* JOURDAN (1987), p. 103 (*supra* footnote 111).

40. Effects of the Revolution. The precedents of *service public* were not significantly altered by the French Revolution.[114] The three main pillars already settled (provision by a public authority, of a service of public interest to the general public, under the rule of public law), had to adapt to the new political structures, but were not significantly modified.

First of all, the important change in the nature and principles ruling the exercise of public power legitimated its exercise and therefore strengthened it. The Monarch was substituted by the State, and democracy was introduced in the way decisions were taken. Secondly, subjects became citizens and in this way the role of the public authority as a provider of services to the citizen was also strengthened. Services were not provided to individuals considered as users, as economic units, but to citizens, as political units. The third pillar of the notion of public service, that of Public Law rule, was also strengthened by the Revolution, that made definitive the separation between Public and Private Law. This separation was not so clear within an absolute monarchy, in which the person of the Monarch personified both realities.

The conclusion is that the Revolution only strengthened a substratum which was already existent, since on the one hand, the notion of *service public* was not one of the main elements of the revolutionary theory, and on the other hand, the political reforms introduced by the Revolution only strengthened the characteristics of the *service public* precedents.

41. 19th century developments. The role of the State as the provider of services of general interest was kept limited for most of the 19th century. On the one hand, the State provided the public services inherited from the *ancient regime*, and on the other created a number of new ones, as a response to the development of new technologies. The liberal State inherited structures from

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[114] *Vide* MESCHERIAKOFF (1991), (*supra* footnote 111).

the *ancient regime*, such as revenue monopolies (post, tobacco etc.), alongside other public services, but these were not the main functions of the State, whose fundamental scope was to guarantee the liberty of the citizens. The role of the liberal State was to keep peace and public order, so that liberty of the citizens would not be menaced. When technological and economic progress made possible the creation and development of new products and services which became of general interest, public security recommended, in some cases, State intervention in the field.

As public services increased, they became a more and more important activity of the State. Eventually, together with the police activities, they became the essence of its activity. This evolution was pushed by the socialist movements that were born in the second half of the 19th century, which accelerated the evolution from the State as police to the State as provider of services. This evolution was determined by the traditional link between the concept of public authority and Public law to the provision of services of general interest. But these principles at the same time, were re-enforced by the new situation, and the link between public interest and public authority became even stronger. Socialism was particularly strong at a local level, and one of its main lines of action was the creation of local monopolies in the general interest sectors.[115] This action had strong ideological motivations, but also historical precedents, so was not as difficult to enforce at a local level as it was at the State level.

3.1.2. The *service public* model.

42. The *Ecole de Burdeaux*. By the beginning of the 20th century, there was an important evolution in the notion of *service public*. Jurisprudencial as well of doctrinal evolution enhanced the role of the *service public* notion as

[115] See BIENVENU, J. J. and RICHER, L. (1982): "Le socialism municipal a-t-il existé?", in *Revue Historique de Droit Français et étranger*, no. 64, pp. 205-223.

criterion of attribution of competence to the administrative tribunals and, at a later stage, to the centre of Administrative Law, as it became the legitimisation of public action as well as its limit. This movement took place in France, but it had effects in the rest of the continent, mainly in the Mediterranean States.

The origins of the changes in the role of the notion the *service public* are to be found in the in the *Arret Blanco* judgement by the *Tribunal des Conflits* in 1873.[116] The fundamental purpose of the *Tribunal des conflits*, was to define the field of competence of the administrative tribunals. This was a delicate issue that needed a clear response, which so far had not been found. The judgement stated that "*la règle de notre droit public [...] place dans le domain naturel de la compètence administrative toute les formées contre l'État à raison des services publics*"[117]. In this way, public service became the criterion for the attribution of competence of the administrative tribunals.

The point of departure of the new theory was the traditional doctrine of the separation between the State as public power, and the State as private person. After this common assumption, the *arret* declared that the State as public power was "*chargé d'assurer la marche des divers services administratifs*".[118] The tribunal drew a necessary link between the State and the provision of public services, in such a way that the provision of public service would necessarily be in the hands of a public administration, that would do so in the exercise of its public power (*puissance public*). The Tribunal not only made this assumption, but also established such a strong link between both notions, that public service became the reason of the attribution of competence for the administrative tribunals.

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[116] *Vide* MESCHERIAKOFF (1991), p. 32 (*supra* footnote 111).

[117] *Arret Blanco*, D 1873 III, 153.

[118] *Arret Blanco*, D 1873 III, 17.

Public service as the criterion of the attribution of competence was successful, but it was ignored by the doctrine for thirty years. It was Leon Duguit and the *Ecole de Bourdeaux*, who took the notion of public service as being central to the theoretical construction of Administrative Law and developed it to its final extremes. For Duguit the *service public* was both an objective reality the necessary activity of the Government in order to achieve the *solidarité social* (this social solidarity was the centre of the discourse, a concept difficult to define, a characteristic construction of the philosophy of the end of the last century), and also an abstract notion, that had no material content, in the sense that it had to be defined for each society, according to its own notion of *solidarité social*.[119]

This notion of public service was to become the centre of the concept of State. "*L'État n'est pas [...] une puissance qui commande, une souveraineté; il est une cooperation de services publics organisés et controlés par des gouvernants*".[120] Public service became the legitimising notion of the power of the State, its foundation and its limit. As it was said by Gaston Jèze, one of the main academics of the *Ecole de Bordeaux*, "*le service public est la pierre angulaire du droit administratif*".[121] By 1920, in France, the notion of public service was necessarily linked to the State, and was to become the "*pierre angulaire*" of Administrative Law, the criterion of attribution of competence for administrative tribunals, and the legitimisation of the power of the State.

43. First crisis and resurrection. Three elements defined the concept of public service in 1920. Firstly, the service was to be provided by a public

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[119] "*toute activité dont l'accomplissement doit etre assure, reglé et controlé par les gouvernants, parce que l'accomplissement de cette activité est indispensable à la realisation et au developement de l'interdependance social, et qu'elle est de tal nature qu'elle en puet etre realisé completement que par l'intervention de la force gouvernante*", DUGUIT, L. (1928): "*Traité de droit constitutionnel*", vol. II, Ancienne Librairie Fontemoing & Cie., Paris, p. 61.

[120] *Ibid.* DUGUIT (1928) p. 59.

[121] In AUBY, J.M. and DUCOS-ADER, R. (1973): "*Grands services publics et enterprises nationales*", two volumes, Presses Universitaires de France, Paris, vol. 1, p. 25.

authority. Secondly, it was to be ruled by Public Law. Thirdly, its function was to ensure the provision of a service of general interest. The crises of the concept of public service started in the 20's, when new structures appeared, and on the one hand, it was provided by public authorities under Private Law, or, on the other hand, private persons, started to provide public services. The content of the *service public* notion was emptied, and the concept entered into crisis.

The first crisis of the concept of *service public* was the provision of services of general interest by public authorities, but under the legal regime of Private Law, instead of following Public Law. The first sign of this novelty appeared as early as 1903, with the *arret Terrier*. In this case the *Tribunal des Conflits* stated that "*il peut se faire que l'administration tout en agisant non comme personne privee mais comme personne publique, dans l'interet d'un service public proprement dit, n'invoque pas le benefice de sa situation de personne publique et se place volontairement dans les conditions du public, soit en passant un des ces contracts de droit commun [...] soit en effectuant une de ces operations courantes que les particuliers font journellement*".[122] This was a clear change in the jurisprudence of the Court, a complete break from the *arret Blanco* doctrine. This case was followed by others,[123] but it is only in 1921, with the *arret Bac d'Eloka*, that the provision of public services by public authorities under Private Law, became widely accepted. The difference between *services public administratives* and *services publics industriels et commercaux* was then developed.

The second crisis was the "privatisation" not only of the legal regime but also of the provider of the service. This meant that either a public authority or a private person, under concession, license or other mechanisms, could provide a service of general interest. This was a very slow evolution, which increased its

[122] *Arret Terrier*, D 1904 III, p. 66, *vide* in MESCHERIAKOFF (1991), p. 37 (*supra* footnote 111).

[123] *Arret Compagnie d'Assurances Le Soleil* D 1912 III, p. 89, for instance.

importance as time passed. These cases became very common by the 1920s and 1930s, when public authorities decided to diversify the structures of the numerous public services in order to improve their quality by adapting them to their function. The provision of public services by private persons involved different structures. However a common element was the definition of strict mechanisms of control by the public authorities of the activities of private persons. The act of concession was always linked to the imposition of obligations, as well as the grant of privileges, in order to ensure the provision of the service. The content of the obligations depended on the particular characteristics of the service. General rules were never developed on the matter.

As a result of this process of "privatisation" of the notion of *service public*, two out of the three original elements of the notion were relativised. The last element, that of general interest was the vaguest. The notion of public service lost its content and entered into a crisis.

With the development of the welfare state, the expression *service public* again became of common use. The doctrine had major problems in defining its content, but politicians and trade unionists amongst others, used the term frequently. This process of the recuperation of the term *service public* was observed with curiosity by researchers, who referred to it as a "*lazare juridic*".

The role of the notion of public service as the centre of Administrative Law, or its use as the criterion for the attribution of competence to administrative tribunals is a French specificity. Nevertheless, it has had a major impact in all the States that shared a common legal culture, such as Belgium, Greece, Italy, Portugal or Spain.

3.1.3. The notion of *service public*.

44. Elements of the notion of *service public*. It is extremely difficult to define the content of the concept of *service public*. There are several reasons

for this. First, the concept had a different content in every nation.[124] The second is that, historically, the role of the notion has also evolved within every country, having different contents along history, as it has been seen in the French case. The result has been a very wide notion, with a very diffuse meaning. Researchers have often refused to offer a definition.[125] Even if a definition has not been reached, researchers have analysed the elements that are relevant of the concept of public service, and agreement has been reached in the definition of two main elements.[126]

The first element that most researchers have recognised as the essence of the notion of *service public*, is that the sector is "reserved" to public authorities, in such a way that private persons can only participate in the sector if a concession is granted.[127] As has been shown, this organic element of the notion of public service has suffered a deep transformation. From the necessary direct provision[128] to the current regime of concessions, which in certain cases supposes a very light control on the private providers of the service "reserved" to the State.

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[124] See CEEP (1995): "*Europe, concurrence et service public*", Masson, Paris, pp. 109-176 for a comparative analysis of the notion in Italy, France, the Netherlands and Spain.

[125] For instance: "*le concept de service public est sature de significations multiples qui se superposent, s'entrecroisent, renvoient les unes aux autres et entre lesquelles le glissement est constant*", CHEVALLIER, J. (1987): "*Le service public*", PUF, Paris, p. 3.

[126] See for instance two recent definitions: "*le service public désigne une activité d'interêt général (element fondamental qui illustre le caractere materiel et finaliste de la notion), prise en charge par une personne publique (élément réducteur qui en atteste le caractère organique); cette prise en charge est perceptible à certain indice*", *in* TRUCHET, D. (1982): "Label de service public et statut du service public", *Actualité Juridique, Droit Administrative*, no. 120 January, p. 428, and "*maîtrise publique assumée par la puissance publique selon différentes modalités (tutelle, maîtrise d'ouvrage, réglementation, tarification, financement), en response aux spécificités et au caracter d'interêt général de la mission*", this last definition was offered by the French government in its proposal for an European Cart of public service, 1993.

[127] This is particularly clear in the Spanish notion of *service public*, whose main element is the *publicatio* or declaration of reserve of the activity for the public authorities, understood almost as an appropiation of the activity, see GARRIDO FALLA, F. (1994): "El concepto de servicio público en derecho español", in *Revista de Administración Pública*, vol. 135, pp. 7-35.

[128] The preamble of the French Constitution of 1946, which is considered a part of the current constitution, states: "*tout bien, toute enterprise, dont l'explotation a ou acquiert les characters d'un service public national ou d'un monopole de fait doit devenir proprieté de la collectivité*".

Secondly, as in the case of the US, the concept of public service requires the existence of a general interest. This material element of the notion of pubic service is, nevertheless very vague. The definition of what is to be considered the general interest is in the hands of the legislature, and it is for this reason that the notion of public service has a strong political character.[129]

As a result of its evolution during this century, both elements of the notion of public service have suffered a process of dilution and public service has become, according to certain researchers, a mere "label",[130] a myth with a high political content but very little legal consequences. *Service public* has become a common expression with a diffuse content, which is useful to legitimise any public intervention.

45. Service public principles. It has always been considered that the mere presence of the State, when directly providing the service, would ensure the satisfaction of the public needs. It was never considered necessary to develop a set of obligations connected to the notion of *service public*. Instead of obligations, researchers developed a set of principles that were to rule the provision of public services by public authorities. Jurisprudence was later developed adopting these general principles. These principles were adapted from general principles of constitutional law, to the particular case of the public services that, in any case, were considered a sector of Public Law. These principles are known as the *lois de Rolland*.

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[129] *"la notion de service public est éminemment politique"*, in BELLOUBET-FRIER, N. (1994). "Service public et droit communautaire", in *L'Actualité juridique- Droit administratif*, 20 April 1994, pp. 270-285, Paris, p. 270.

[130] *"il n'y a pas de notion du service public; le mot recouvre des realités juridiques variables selon les besoins propres du "locuteur" [...] anotre avis, cést un label accordé a une activité, [...] apparait comme un mythe qui, d'une part legitime [...] L'action public, et d'autre part, croisé avec l'idee de puissance publicque, fonde l'ideologie du droit administrative actuel"*, in TRUCHET, D. (1982): "Label de service public et statut du service public", *Actualité Juridique, Droit Administrative*, no. 120 January, p. 430.

Equality was the first of these principles governing the provision of public services. This principle had an obvious constitutional origin. Equality in the provision of public services, had the same meaning as in constitutional law. It supposed the same treatment in equal situations. This general principle of law has been applied by the French *Conseil d'État.*[131]

Continuity is also a traditional principle in the provision of public services. If a service is considered of general interest, it is because it is considered of basic importance for the community, and therefore, there is the need to ensure its continuity. This principle has been enforced by the French *Conseil d'État* in cases of strike in public services.[132]

Adaptation is the last traditional principle. This principle tries to ensure the satisfaction of the basic needs. Only the transformation across time, adapting the provision of the service to the new conditions can ensure the satisfaction of public needs.

As it has been said, the principles of public service are general principles of law which apply to the common activity of the administration and obviously apply also when the administration is providing a public service. The question is whether these principles apply also to the provision of public services by public authorities under private law and indirectly by private persons. The concession of a public service is usually accompanied by a definition of the obligations and privileges parallel to the concession, however no general obligation has been developed.

[131] For instance C.E. February 1, 1985, *Union departamentale des consommateurs de Paris*, in which the charge of a lower price for electricity in towns nearby a nuclear plant, was considered contrary to the principle of equality in the provision of public services.

[132] For instance, C.E. July 15, 1979 in a case related to broadcast service.

3.2. COMPETITION LAW IN EUROPE.

46. General. European competition Law does not have such a long tradition as antitrust in the US.[133] If antitrust has its earlier precedents in English Common Law and is intrinsically connected with the American political and legal tradition, competition Law appeared in Europe, and particularly in Germany, after World War II, as a reaction to the excesses produced by the local political tradition. [134]

The German model of industrialisation, which was followed in other European nations was coherent with the interventionist political tradition and granted a primary role to the public authorities as well as a close connection between those authorities and the leading industry groups. Particularly interesting was the favourable approach to private cartels as a mechanism of control of an economic sector by the public authorities. According to a significant portion of the political and economic commentators, such connections facilitated the rise of the Nazi movement in Germany and the subsequent dramatic events.

A small group of academics at the University of Freiburg witnessed the process of decadence of the Weimar Republic and the rise of Nazism, and reflected on the negative effects of the restriction of competition in the market, the concentration of private economic power, and its connections with political power. The result was the formation of a coherent body of doctrines evolving around the role of the State in economic activity, and in particular the need to ensure the effectiveness of competition mechanisms in order to avoid the concentration of private economic power and the mutual interference between private economic power and public political power. Thanks to the compatibility

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[133] *Vide supra* Chapter 2.2. The Origins and Evolution of Antitrust.

[134] See AMATO, G. (1997): "*Antitrust and the Bounds of Power. The dilemma of liberal democracy in the history of the market*", Hart Publishing, Oxford, p. 40.

of their principles with the ideology of the occupant forces, the *Freiburger Ordoliberalen* School[135] acquired a prominent intellectual and political position under the American occupation following the end of the war,. As a result, the first Competition Act of the continent was adopted in Germany in 1957.

The intellectual principles of the *Freiburger Ordoliberalen* School saw some diffusion among academist in some European nations. Nevertheless, the most important effect of the School throughout the Continent was the adoption of the principles of competition and the definition of antitrust provisions in the European Economic Community Treaty. This was due to the position of the German authorities in the negotiations for the drafting of the Treaty.

Despite the initial restraints on competition policy imposed by the political traditions of the Member States and the existence of important exceptions in the Treaty to the mechanisms of free competition in the market, competition rules "proved to be as magic boxes, capable of expanding their content, where initially conceived in a much more limited context".[136]

Competition policy benefited from the political impulse towards the integration of the markets, due to the fact that it provided a powerful instrument against barriers to such integration.[137] In this way, competition policy has effectively become one of the most important policies of the European Union, and competition acts have been adopted in all the Member States.

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[135] See GERBER, D. (1994): "Constitutionalizing the Economy: German Neo-Liberalism, Comparative Law and the 'New' Europe", in *The American Journal of Comparative Law*, vol. 42, no, 1, pp. 25-84.

[136] *Vide* AMATO (1997), p. 43 (*supra* footnote 134).

[137] See EHLERMANN, C. D. (1992): "The Contribution of EC Competition Policy to the Single Market", in *Common Market Law Review*, vol. 29, p. 257.

3.3. THE PROCESS OF LIBERALISATION.

3.3.1. Liberalisation, de-monopolisation, privatisation and competition.

47. Criticisms arrive in Europe. American criticisms about the excessive public intervention in the economic activity also reached Europe.[138] Public monopolies were accused of inefficiency, poor service, high prices and of obstructing the competitiveness of the European economy. At the same time, most of the arguments made against regulatory intervention could be extended to public monopolies, which also had a strong tendency to be captured by managers, politicians and trade unions, and were difficult to control and to co-ordinate by Parliaments and the Judiciary.[139] European societies never reached a wide consensus on the option of desestalisation, as happened in the USA.

It was in the UK that public intervention was first considered an obstacle to economic growth, and privatisation and de-monopolisation were first undertaken.[140] In the 1990s it has been widely shared, also in the Continent, that public monopolies in the general interest sectors were inefficient, and public interest could be protected through less restrictive instruments.

An important element in the process of the reform of public intervention in the European economy has been the role of the European Union institutions. Firstly, the process of market integration forces the gradual elimination of national monopolies, as they automatically divide the market along national borders. Furthermore, the process of political integration promoted the substitution of national direct intervention by indirect intervention designed at a

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[138] *Vide supra* Chapter 2.3. The Process of Deregulation.

[139] See MAJONE, G. (1995): "*Regulating Europe*", Routledge, London, p. 18, and MAJONE, G. (1996): "*La Communauté européenne: un Etat régulateur*", Montchrestien, Paris, p. 18.

[140] See SWANN, D. (1988): "*The Retreat of the State. Deregulation and Privatisation in the UK and US*", Harvester-Wheatsheaf, London.

Community level. Since Community structures are weak, in the sense that they lack not only political power but also the infrastructure to develop a direct intervention in all the Union, Community institutions have opted for the development of an indirect control of economic activity through regulatory techniques, which eliminates the need of national direct intervention.

48. Liberalisation. The process of the substitution of the traditional *service public* direct intervention through national public monopolies, by competition in the free market between an unlimited number of private companies under indirect intervention by the public authorities, can be denominated as the liberalisation of the European markets.[141]

This process includes three different but connected processes. On the one hand, public authorities have de-monopolised the markets, putting an end to the exclusive or special rights that restricted market access to other operators. On the other hand, public authorities have privatised the assets used for the direct provision of the services, in what has been named a process of privatisation. Lastly, different regulatory schemes have been often introduced in order to facilitate the transition from monopoly to effective competition.

The process of liberalisation of the European economy has been more complicated than the process of deregulation in the United States. The first reason is that liberalisation is in contradiction with some of the most established dogmas of the European political tradition, particularly with the philosophy of the direct defence of the public interest by the public authorities as mechanisms to elevate public action over the private interests. Secondly,

[141] Some authors use the term deregulation to denominate the European process of reform of public intervention in the economic activity. We do not completely agree, since we prefer to keep the term "deregulation" for the American process of reform of their traditional regulatory intervention model. The term "deregulation" can lead to confusion since the elimination of public monopolies does not imply a reduction of public intervention but a modification in the mechanisms that can even make the intervention more complicated. That is why a significant number of researchers preferred the terms "re-regulation" or even "neo-regulation".

liberalisation is incompatible with the traditional model of public intervention the *service public*, and its main mechanisms, the public monopoly. As a result, a completely new model of public intervention, based on indirect intervention compatible with the free market mechanisms has to be established, and new institutions and mechanisms have to be defined.

3.3.2. Renewal of the *service public* concept.

49. The defendants of the notion of service public. Challenges to the notion of *service public* have been rebuted by a conjunction of forces. Firstly, academic research, mostly in France, has been developed, trying, on the one side, to renew the notion of *service public* in order to improve its internal coherence and its economic efficiency and, on the other side, criticising the position of the Community institutions.[142] The French *Conseil d'État,* for instance, in the *Rapport Public* of 1994,[143] developed a strong defence of the notion of *service public*. A deep *renouvement* was advised in order to face criticisms about the economic performance and the political control of the public monopolies. Secondly, powerful public monopolies are also intervening in the debate, for instance through the *Centre Européen des Entreprise á Participation Publique* (CEEP).[144] Lastly, some Member States, led by France,[145] made proposals, even for a reform in the Treaties.[146]

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[142] See three dossiers with contributions from different authors published in the last years: VV.AA (1994): "Service public, service universel", in *Reseaux*, vol. 66, pp. 1-178; VV.AA (1995): "Le service public et la construction communautaire" in *Revue Française de Droit Administratif*, vol. 11, no. 2 pp. 291-342, and no. 3, pp. 449-503; and VV.AA. (1996): "Services d'intérêt économic général", in *L'Actualité Juridique. Droit Administratif*, vol. 52, no. 3, pp. 171-191.

[143] *CONSEIL D'ÉTAT* (1995): "Service public, services publics: déclin ou renouvement?", in *Rapport Public 1994*, Etudès et Documents du Conseil d'État, no. 46, La Documentation Française, Paris.

[144] CEEP made an ambitious proposal for the reform of the Treaty, with the creation of a new chapter in title V, and a new article devoted to the defence of *service public*, in CENTRE EUROPÉEN DES ENTREPRISES À PARTICIPATION PUBLIQUE (1995): "*Europe, Concurrence et Service Public*", Masson, Paris.

[145] During its presidency in 1993, the French republic presented a memorandum to the Commission with the proposal of elaborating an European Charter of the public services.

Arguments obviously are varied, but a common line of defence can be found. On the one hand, there has been an effort to renew the notion of *service public*, making it more acceptable for jurists, economists and consumers. On the other hand there is a critic to the position of Community institutions.

50. Renewal of the notion of service public. The first movement of the defendants of the *service public*, led by the *Conseil d'État*, has been to review the concept of *service public* and the principles attached to it, in order to face criticisms about the lack of coherence of the concept, about the lack of efficiency and about its implicit political accountability.

On the one hand, the concept of *service public* has been redefined in order to face the criticisms of lack of internal coherence of the concept. The initial position has been the distinction between *service public* and a series of institutions that, in the past, have been necessarily linked to the notion: monopoly, public property, perequation, *fonction public*, or public domain. This is only a distinction, in the sense that these are mechanisms compatible but not necessarily linked with the notion of *service public*. The following step has been to redefine the concept of *service public*. If the strict notion of public service required the direct intervention of a public authority, under a public law regime, the broader notion requires only some kind of public intervention, added to the regular control of economic activity by the State. According to the *Conseil d'État* and most of the doctrine, "*il en saurait y avoir service public sans mâitrise ou régulation publique et plus précisément sans mise en oeuvre de procédés de régulation autres que ceux qui sont normalment à la disposition de la puissance public [...] dans ses rapports avec le tout-venant des acteurs économiques*". Public intervention could go from an exclusive right granted to

[146] See MONTERO PASCUAL, J. J. (1997): "I monopoli nazionali pubblici in un mercato unico concorrenziale. Evoluzione e riforma dell'art. 90 del Trattato", in *Rivista Italiana di Diritto Pubblico Comunitario*, vol 7, no. 3-4, pp. 663-672.

a public undertaking, to a mere license regime and a light control of the activities of the private undertakings in the sector.

On the other hand, in order to face criticisms of inefficiency and "public failure", the traditional principles ruling the public intervention. (equality, adaptation, and continuity) have been strengthened, and new principles have been introduced (neutrality, participation, transparency, responsibility, simplicity and accessibility). Adaptation and continuity should improve the economic efficiency. Equality, transparency and participation would improve the situation of the citizen/consumer before the providers of the services, while transparency and responsibility would avoid the "capture" by politicians and managers.

3.3.3. *Service public* and Community Law.

51. The intervention of the Community institutions. Article 86 (former Article 90) of the European Community Treaty is the key provision defining the balance between the interest of further integrating the European markets, and the interest to maintain Member States' rights to create national public monopolies.[147] Originally, the mere existence of national public monopolies was not forbidden, but for the first time, limits to the exercise of the exclusive rights were imposed on the States. Article 86 presupposed the legality of the existence of the exclusive rights, and even if the exercise would be contrary to some provision of the Treaty, Article 86(2) provided an special regime allowing restrictions to movement and competition within the common market, if necessary to ensure the provision of services of general interest. The approval of the Single European Act altered the balance of interests, strengthening the goal of reaching a single market, bringing about an evolution in the approach of

[147] See BLUM, F. and LOGUE, A. (1998): "*State Monopolies Under EC Law*", Wiley, Chichester.

the European Commission and the European Court of Justice towards national public monopolies.[148]

Commission decisions[149] and directives[150] passed through the Article 86(3) procedure (which allowed the Commission to pass directives without the intervention of the other community institutions), and relevant judgements of the Court[151] in the late 1980s beginning of the 1990s, extended the incompatibility with the Treaty from the exercise to the existence of the exclusive rights granted by a public authority. Community institutions commenced to judge the mere grant of the exclusive and special rights,[152] and declared some of them contrary to the Treaty (whether to provisions defending the four freedoms or to provisions defending competition). Not only the application of Community Law was strengthened, but the provision in Article 86(2), from an special regime passed to be an exception, to be applied restrictively.[153] In such a way, the exception would only apply when the

[148] *Vide* MONTERO PASCUAL (1997), pp. 663-668 (*supra* footnote 146).

[149] Commission decision of 22 June 1987, OJ 1985 L 194/28 and Commission Decision of 20 December 1989, OJ 1990 L 10/47, are only some examples.

[150] Commission Directive 88/301/EEC, of 16 May 1988, OJ 1989 L 131/73 and Commission Directive 90/388/EEC, of 28 June 1990, OJ 1990 L 192/9, the telecommunications directives, declared contrary to the Treaty the telecommunications terminals and telecommunications services monopolies.

[151] Case 202/88, *France v. Commission*, [1991] ECR I-1223, of 19 March, Case 41/90, *Klaus Höfner and Friz Elser v. Macroton GmbH*, [1991] ECR I-1979, of 23 April, Case 260/89, *ERT v. Dimotiki*, [1991] ECR I-2925, of 18 June, Case 179/90, *Merci Convenzionali Porto di Genova v. Siderurgica Gabrielli*, [1991] ECR I-5889, of 10 December, Case 18/88, *RTT v. GB-Inno-BM*, [1991] ECR I-5941, of 13 December and Joined cases 271, 281 and 289/90, *Spain v. Commission*, [1992] ECR I- 5833, of 17 December.

[152] The "unavoidable abuse" doctrine was elaborated in order to declared incompatible with the Treaty the mere existence of the monopolies, see EHLERMANN, C. D. (1993): "Managing Monopolies: The Role of the State in Controlling Market Dominance in the European Community", in *European Competition Law Review*, vol. 14, no. 2, pp. 61-69.

[153] For a negative vision of this process see DE LA QUADRA-SALCEDO, T. (1995): "*Liberalización de las telecomunicaciones, servicio público y constitución económica europea*", Centro de Estudios Constitucionales, Madrid.

application of Community Law would make impossible the provision of the service of general economic interest, and not only obstruct it.[154]

52. Confrontation. Defendants of the notion of *service public* did not accept the interference of Community institutions in the Decisions of Member States with regard to their intervention in the economy. Instead of adapting the notion of *service public* to the constraints of Community Law (as the *Conseil d'État* had done with regard to the criticism in respect to internal coherence and economic efficiency), most of them have pled, unsuccessfully, for the elimination of those constraints, whether it be through a change in the application of Article 90, or through a reform of the Treaty having the same effect.[155]

Service public interventions are necessary, they claim, to ensure the goals of the general interest, because market mechanisms do not take into account some of these goals. This public intervention might be contrary to a Treaty whose values are competition and freedom of movement, but necessary to maintain social cohesion. As a result, exceptions for the application of the competition and freedom of movement principles need to be provided.[156]

53. *Le dernier crisis du service public.* It is the very same root of the notion of *service public*, as it has been defined by the *Conseil d'État*,[157] which is in conflict with Community Law. The essence of the *service public* notion

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[154] The most recent judgements of the Court might have altered the strict application of the exception in article 90(2), nevertheless, it has to be taken into account that those were cases decided under article 177, and in sectors were community action has not introduced regulation in the sector. See Case 320/91, *Regie des Postes v. Paul Corbeau*, [1993] ECR I-2533, of 19 May; and *Commune de Almelo and others v. Energiebedrijf IJsselmij*, [1994] ECR I-1477, of 27 April.

[155] Most of the reforms suggested tended, through different mechanisms to strenght the value of public intervention in defence of the general interest. There was a proposal by the CEEP to annex a Charter of Public Service to the Treaty, as well as to reform the actual provisions ruling the issue, adding, for instance, a new article 94B, with a concrete provision defending *service public*. The Amsterdam Treaty has not adopted any of these solutions, but merely the option proposed by the Commission.

[156] The minutes of the European Parliament sitting of Wednesday 4 September 1996, on the issue perfectly reflect the ideological conflict in Europe.

relies on the almost omnimodous power of the State to define a special legal regime for certain activities, excluding the regular development of the activity by private operators under Private Law, at the same time that special powers are ensured to the public authorities. It is for the State to decide the level of interference, which ranges from the monopolisation of the activity, to the lightest control of the private actors' activity. Traditionally, the only limitation to the State in this respect was the very devaluated constitutional right to free enterprise.

The apparition of a new supra-national entity, the European Community, with its own legal order characterised by its supremacy over national laws, introduced a new and fundamental limitation to the power of the State. Furthermore, the fundamental scope of the European Community is the integration of the European nations, particularly the integration of the different national markets. In this respect, public restriction to private economic activity tends to obstruct market integration, and for this reason, they are in principle contrary to one of the fundamental pillars of the Community legal order.

Community institutions have fundamentally declared the incompatibility of the granting of exclusive rights in certain sectors, one of the traditional mechanisms of public intervention, with the EC Treaty. The very same notion of *service public* has not been expressly declared incompatible with Community Law. Nevertheless, the introduction of the judgement on the power of the State to exclude any activity from the regular Private Law regime, makes the almost omnimodous title of intervention incompatible with the EC Treaty.

The creation of a strict legal limit to the power of the State to exclude an activity from the general regime of competition in the market, modifies the centre of interest in the study of public intervention in the economic activity.

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[157] *Vide CONSEIL D'ÉTAT* (1995) (*supra* footnote 143).

The centre moves from the legislative declaration of a service as *service public*,[158] to the specific legal regime imposed to a service considered of general interest, due to the necessary evaluation of its compatibility with the Community legal order. As a result, the category of *service public* should be replaced by different categories of public intervention, according to their principles, mechanisms and institutions. This does not mean that all the *service public* legal regime should be eliminated. On the contrary, the traditional principles defined for the category are still in place for many of the public intervention institutions, as well as the many of the principles recently defined by the administarativist doctrine. Nevertheless, the object of research should be focused on the specific public intervention regimes, particularly in those regimes recently created, such as the mechanisms for the indirect defence of the general interest in liberalised sectors.[159]

3.4. PUBLIC INTERVENTION IN EUROPEAN TELECOMS.

3.4.1. Origins of the telecommunications markets in Europe (1876-1900).

54. Telegraphy. The structure of the European telecommunications industry in its earlier era[160] was highly influenced by the decisions adopted for the management of the first telecommunications device, the telegraph. In the

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[158] This is particularly clear in relation to the Spanish notion of *servicio público*, which main element is the *publicatio*, *vide* GARRIDO FALLA (1994) (*supra* footnote 127).

[159] See MONTERO, J. J. and BROKELMANN, H. (1999): " *Telecomunicaciones y televisión. La nueva regulación en España*", Tirant lo Blanch, Valencia, pp. 46-48.

[160] The following pages on the evolution of public intervention in the European telecommunications sector will be mostly centred in the French case, the one that more clearly reflects the principles behind such intervention, but references to the British, German and Spanish experiences will be continuous. In the necessarily superficial review of such evolution, we intend to avoid a normative approach, and even at the risk of providing a simplistic image, we intend to show the contradictions between the discourse of the public monopolies against de-monopolisation, based on the need of the public monopolies in order to guarantee the provision of services of general interest, and the historical role of such monopolies in their national markets.

UK the exploitation of the activity was initially in hands of private undertakings. It was only thirty years after the installation of the first commercial line that the network was nationalised.

In France and in Germany the provision of the service had been monopolised from the beginning by the public authorities. Furthermore, the first lines were built for the exclusive use of governmental departments, mostly the military in Prussia and the *Ministere de l'Interieur* in France. It was only at a second stage that the telegraph lines in the hands of the State were commercially exploited.[161] In 1852 (thirteen years after the installation of the first line in Europe) it was stated that the telegraph in the continent "was more a weapon in the hands of Government than a means of promoting social and commercial communication for the community".[162]

55. Telephony. When Bell's invention was introduced into Europe, most of the national Governments decided to include such service under the exclusive right for the provision of the telegraphy service. In Germany, the Post and Telegraph Administration monopolised the service from its origins and no private activity in the sector was never allowed.[163] In France, in 1879 the Ministry of Posts and Telegraph adopted a decree granting the concession of the right to provide telephone service, to a private company.[164] This meant that telephony was included in the monopoly enjoyed by the Post and Telegraph administration, but at the same time showed the will of the Administration not to operate the service, unless at that moment. In the UK the extension of the exclusive right from telegraphy to telephony was challenged in Court by

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[161] *Vide* BROCK, G. (1981): "*The Telecommunications Industry. The Dynamics of Market Structure*", Harvard University Press, Cambridge, MA, for the history of telegraphy in the leading European States.

[162] E. Highton in "*The Electric Telegraph*", quotation from FOREMAN-PECK, J. and MILLWARD, R. (1994): "*Public and Private Ownership of British Industry, 1820-1990*", Claredon Press, Oxford.

[163] See LIBOIS, L. J. (1983): "*Genèse et criossance des telecommunications*", Masson, Paris, pp. 268-272.

private operators who desired to operate the service. Courts finally recognised the Post Office exclusive right.[165]

From its very origin the strategy of the public authorities was to control the development of the industry, even if it could not be done through the direct exploitation of the networks, due to the financial problems of the State.

During 1880's the main characteristic of the sector in Europe was confusion. Most of the national Governments granted licensees to private operators for the exploitation of the service, but under restrictive conditions.[166] At the same time, the Post and Telegraph Administrations started to invest for the development mostly of long distance network. The risk of nationalisation following the German model was always present. As a result, the development of the network under such difficult conditions was very poor. Prices were very high because private operators were pushed to be interested in the immediate recovering its investment rather than in developing a long-term policy of construction of a network. This led to dissatisfaction of the public with private telephone operators. At the same time, public authorities lacked the financial resources to build a comprehensive network, "their whole attitude seemed to have been dictated by the one purpose to evade the risk of introducing the new service by shifting the responsibility to private promoters. At the same time they protected themselves against unexpected success by making the term of the franchise short".[167]

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[164] See BAKIS, H. (1987): "Formation et développement du réseau téléphonique français", in *L'Information Historique*, vol. 49, p. 31. 31-43

[165] See ROBERTSON J. (1947): "*The Story of the Telephone*", Pitman & Sons, London.

[166] For the French case *vide* BAKIS (1987), (*supra* footnote 164); for the Spanish case see OTERO CARVAJAL, L. (1993): "El teléfono. El nacimiento de un nuevo medio de comunicación. 1877-1936", in "*Las comunicaciones en la construcción del Estado moderno en España 1700-1936*", MOTMA, Madrid.

[167] HOLCOME, A.N. (1911): "*Public Ownership of the Telephones in the Continent of Europe*", Harvard University Press, Cambridge MA.

3.4.2. Public monopolies (1900-1987).

56. General. Around the turn of the century most of the European States opted for the German model of the monopolisation of the telecommunications activity by the Post administration and the nationalisation of the private operators active in their national markets.[168] The French nationalisation is particularly interesting, as it shows the reasons behind such decision. In 1889 the *Chambre des Députés,* following the Report presented by the *Député* Cochery supporting the governmental law proposition, decided to nationalise the telephony network with a strong parlamentary majority.

M. G. Cochery (son of the 1878-1884 Post and Telegraph Minister) was the *Depute* in charge of presenting the report of the Parliamentary Commission about the Proposition of the government to nationalise the telephone company. According to this report there were three reasons for the nationalisation. Firstly, the Commission considered that granting a long concession to a private undertaking, in a technologic sector in fast development would mean *"s'exposer ou bien à aliener des droits naturellement réservés à l'État, à abandoner une partie des attributions dont il en peut se dépuiller, ou bien à interdire au public l'usage des progrès réalisés".*[169] This is the basic reason for the monopolisation. The telecommunications sector was of strategic importance, and for these reason it was reserved for the State, not because it had to offer an efficient service to the citizens, but because it was a strategic sector in which the private interest could not defend the interest of the

[168] This was the case in the UK, where the sector was nationalised in 1911, *vide supra* footnote 165, ROBERTSON (1947), pp. 1-89. There were, nevertheless, some exceptions, such as the Spanish case. monopolisation of the sector took place on ly in 1924 and the monopoly was not ensured to the public authorities but to a private company controlled by the foreign operator, ITT, *vide* OTERO CARVAJAL (1993), (*supra* footnote 166).

[169] See the Report to the Chamber from the Parlamentary Commission studying the law proposition on the nationalisation of the telephone industry Commission, in BUREAU INTERNATIONAL DES ADMINISTRATIONS TÉLÉGRAPHIQUES (1889): "Les Telephones en France", *Journal Télégraphique*, vol. 13, no. 7, p. 143.

collectivity. Secondly, it was maintained that telephony was competing with the public monopoly of telegraphy, and in order to defend this service, telephony would have to be integrated in the public monopoly. Third, the report argues that there are "*inconvenients politiques et d'ordre public*",[170] reinforcing that it is the very same conception of the State, as superior point in which private interests are confronted and the public interest defined.

At that moment the telephony market did not have a natural monopoly structure, since the switching had strong diseconomies of scale, so the natural monopoly argument was not the cause of the nationalisation. Neither public service arguments justified the nationalisation. It was the conception of the role of the State as superior arbiter of the private interest, defendant of the public interest, together with some practical considerations on the future of the telegraph monopoly, that forced the State to monopolise the telecommunications market, but not the public service nature of the sector.

57. The public monopoly before World War II. The French post, the telegraph and the telephone industries were, after 1889, controlled by a national public monopoly in the hands of the Post, Telegraph and Telephone Ministry. Nationalisation did not bring an improvement of the conditions offered to the users. The main problem was that the State did not consider telecommunications a priority. As a result the public monopoly disposed of very little finance for the development of the network. Public intervention not only did not improve the service, but also produced some criticisms on the way it was managed. The Cochery family was accused of the absolute domination of the sector by the *École polytechnique.*[171] Problems of capture by the *ellite* were frequent since that time.

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[170] *Ibid.* BUREAU INTERNATIONAL DES ADMINISTRATIONS TÉLÉGRAPHIQUES (1889), p. 143.

[171] *Vide* LIBOIS (1983), p. 211 (*supra* footnote 163).

From 1889 to 1892, all network extensions were financed by local authorities and users, who were required to provide finance for the works, being the payments returned later.[172] This system (*avances remboursables*) was maintained until World War I for the extension of the network in rural areas, in violation of the *service public* principle of equality. The renewal and extension of the telephone network was difficult to finance and as a result the extension was much slower than in the USA,[173] and the quality minimal. Direct funding by the State budget was later introduced, but telecommunications were never a priority, causing a chronic under development of the French network. The monopolist policy in rural areas was especially contrary to the principles of *service public*. Whilst in the competitive American market, 39% of the farms had a telephone in 1920,[174] the French monopolist required local authorities and users to finance the extension of the network to rural areas.

In the beginning of the 1920s the extension and the quality of the French telephone network were so poor, that people started to demand the elimination of the public monopoly. In 1922, the *sous-secretaire d'État aux Postes et Telegraphe* recognised that the user "*résume son mécontent dans cette invective: si l'État est incapable d'exploiter le téléphone, qu'il passe la main à l'industrie* privée".[175]

The clear conclusion is that during the first fifty years of its existence, the telecommunications monopoly did not follow the most basic principles of the *service public*.

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[172] *Vide* BAKIS (1987), p 33, (*supra* footnote 164).

[173] In 1910 the number of telephone station in France was eight times less than in the USA, and slightly lower than the European average. See CHAPUIS, R. (1982): "*100 Years of Telephone Switching (1878-1978)*", North-Holland Publishing Co., Amsterdam, p. 139.

[174] *Vide supra* Chapter 2.4.1. Origins and Free Competition in the US Telecoms Markets (1876-1921).

[175] See LIBOIS (1983), p. 70 for this and other references to the request of privatisation of the telephone industry.

58. The monopoly after World War II. The situation did not change after the war. The first step was the creation of the *Commissariat General du Plan* in 1946, charged with the responsibility of developing a plan of investments for the reconstruction and modernisation of the economy and the infrastructures. Within this framework was created the *Commission de modernisation des telecommunications*. Nevertheless, the telecommunications did not benefit of the public investments in the four first plans. As it was stated: "*Pendant les quatre premiers plans, on a rejette volontairement dans l'ombre d'autres secteurs, car on a estimé qu'il y avait des choses plus urgentes à faire*".[176] This meant that, again, French telecommunications services lagged behind their competitors.[177]

It is only by the end of the 1960s with the fifth and definitely with the sixth and seventh plans, that telecommunications became a priority and massive investments were developed in the sector. It is during this period that universalisation became an objective of the public monopoly, even if it was a long-term one. Investments led to a multiplication of telephone penetration and the automatisation of the network (the two main objectives of the plans), catching up with the European neighbours, even if always remaining behind the USA.[178]

It is only at this late stage, more than eighty years after the creation of the monopoly, that some of the principles of *service public* started to be applied to the sector, and certain mechanisms were introduced to achieve universality. The main mechanism was cross-subsidiarisation. It is only at this point that a conscious policy of differentiation of prices in order to improve penetration was implemented. This policy, nevertheless, just strengthened an existent

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[176] M. Guéna, Minister of the PTT, in LIBOIS (1983), p. 257.

[177] See NOAM, E. (1992): "*Telecommunications in Europe*", Oxford University Press, Oxford, p. 141.

[178] See TUNSTALL, J. and PALMER, M. (1990): "*Liberating Communications. Policy-Making in France and Britain*", NCC, Oxford, p. 147.

tendency. Technological evolution had been reducing long distance services costs dramatically, while the reduction had minor influence in the local service. The maintenance of the price structure naturally produced a divergence from costs, creating a cross-subsidy from long distance to local calls. The option of cross subsidising was just the result of "leaving things as they were", since no serious research on costs was undertaken, and regular adaptation from prices to costs would have been impossible.

3.4.3. Liberalisation of the telecoms markets (1987-1998).

59. Reasons of the liberalisation. By the 1980s the importance of the telecommunications sector in economic life became evident, not only because of its own weight but also because of its effect on the competitiveness of many other sectors. In an advanced economy, information is the most valuable good and having effective systems to handle and transport it became a basic necessity and an indispensable tool for competing in a global market.

The fundamental force of change in the world of telecommunications has been technological evolution. Digitalisation and the development of new carrier techniques (satellite and optical fibres) allowed the convergence of the sectors of telecommunications, computers and multimedia, and an explosion of new services. National monopolies were not efficient in responding to the new demands of the market, particularly high tech, very specialised demand. R&D has become very expensive, in such a way that wide markets are necessary to ensure the profitability of the investments.

At a European level, the need for wider markets, faster introduction of new services and renewal of the network, was observed by the Community institutions as a good opportunity to implement the integration of the markets also in the provision of services of general interest

The technological evolution and the construction of the European single market, together with new political trends in the US and other parts of the

world in favour of less State intervention in the economic activity, have been the forces that have produced the reform of the telecommunications sector.

60. The liberalisation process. The process of reform of the European telecommunications sector has been led by the European Community authorities, and in particular by the European Commission.[179]

The process of reform comprised three parallel processes. Firstly, there has been a process of privatisation of the public provider of telecommunications sector.[180] This was simple in the Spanish case, since the traditional monopolist had always been a private company with a minority share in hands of the State, and one of the principal financing mechanisms was the selling of new stocks. The first Member State which modified the legal status of the telecommunications service provider was the UK in 1981. The telecommunications assets of the Post Office were transferred to a new nationalised corporation, British Telecom, which would later be privatised.[181] Similar procedures were followed in most of the Member States.

Particular difficulties were faced in France, where the political tradition and the strength of the trade unions complicated the process and obstructed the lost of control of the company by the State. Privatisations were the result of the process of transformation of the role of the public authorities in the telecommunications industry. They also provided an income source for Member States in a period of tight budgets due to the evaluation of the deficit

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[179] For a general overview of such process see ALABAU MUÑOZ, A. (1998): "*La Unión Europea y su Política de Telecomunicaciones. En el camino hacia la Sociedad de la Información*", Fundación Airtel Móvil, Madrid; BLANDIN-OBERNESSER, A. (1996): "*Le régime juridique communautaire des service de telecommunications*", Armand Colin, Paris; and MOSTESHAR, S. (1993): "*European Community Telecommunications Regulation*", Graham & Trotman, London.

[180] See CABY, L. and STEINFIELD, C. (1994): "Trends in the Liberalisation of European Telecommunications: Community Harmonization and National Divergence", in *Telecommunications in Transition. Policies, Services and technologies in the European Community*, SAGE, London, p. 45.

[181] See HARPER, J. (1997): "*Monopoly and Competition in British Communications. The Past, the Present and the Future*", Pinter, London, pp. 137-156.

criteria for the Economic and Monetary Union foreseen in the Maastricht Treaty.

Secondly, a Commission-led de-monopolisation process abolished the exclusive and special rights granted by the Member States to their national champions. The de-monopolisation process took place in two phases. The initial phase finished in 1992 with the exclusive rights in the telecommunications terminal equipment and in the value-added services. The second phase extended the abolition to all the exclusive rights in the sector, including voice telephony and infrastructures for 1 January 1998. Member States in general did not oppose the process itself, but the mechanisms employed by the Commission, particularly the Article 86(3) directives, were the object of challenges before the European Court of Justice, which always upheld the Commission's position. Most of the Member States considered the reform of the telecommunications markets structures and the introduction of competition in such markets inevitable. The Community action avoided the confrontation of Member States with national trade unions and national monopolies and the high political costs such conflicts could produce.

The last element in the process of reform was the introduction of a harmonised regulatory framework for the transition from monopoly to effective competition. Different Community directives drawn the basic lines for such transition on issues of high relevance such as interconnection and market access, numbering, rights of way, frequency management and universal service.

61. The first de-monopolisation wave (1977-1992). By the end of 1977 the European Commission created a working group in order to initiate sectorial studies on telecommunications. The first results of such activities was the publication of a Commission Communications to the Council,[182] with the

[182] COM(80) 422 final, Recommendations on Telecommunications, Brussels, 1 September 1980.

proposal to adopt four Recommendations in order to contribute to the developing of a Community-wide market for the European telecommunications equipment industry. The Council did not immediately adopt any Recommendation on the subject, but the Commission continued issuing Communications mostly related to the need of reforming the European telecommunications equipment industry. Throughout the first half of the 80's the Commission, and later the European Parliament and also the Council published different documents related to standard harmonisation in the sector, public procurement and research.

The adoption of the 1985 White Paper on the Completion of the Internal Market, and the reforms introduced by the Single European Act, provided the necessary political support for the Commission to launch a wider debate on the reform of the sector.[183] In November 1987 the fundamental Green Paper on the Development of a Common Market of Telecommunications Services and Terminals[184] was published. This Communications analysed the transformation of the European telecommunications markets, and launched some proposals in order to develop European-wide markets that would allow the European to become more competitive.[185] In consideration of the broad consensus perceived by the Commission on its proposals, the Commission announced its intention to pursue a "rapid full opening of the terminal equipment market to competition"[186] through the publication of a Directive under Article 90(3) EC

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[183] See the effects of the Single Market in the telecommunications markets in BOSSARD CONSULTANTS (1998): "*Telecommunications: Liberalised Services*", The Single Market Review, European Commission, Luxembourg.

[184] COM(87) 290 final, Towards a European Dynamic Economy, Green Paper on the Development of a Common Market of Telecommunications Services and Materials, Brussels 18 November 1987.

[185] See SCHERER, J. (1993): "Telecommunications Law and Policy of the European Union", in *Telecommunications Laws in Europe*, Kluwer, London, pp. 1-28.

[186] COM(88) 48 final, Towards a Competitive Community-wide Telecommunications market in 1992. Implementing the Green paper on the Development of the Common Market for Telecommunications Services and Equipment. State of Discussion and Proposals by the Commission, Brussels 9 February 1988, p. 16.

Treaty, as well as its intention to reach a "progressive opening of the telecommunications services market to competition from 1989 onwards"[187], with the exception of the provision and operation of network infrastructure and, at that stage, of voice telephony service. In parallel, a series of indispensable complementary measures were defined, including the submission of an Article 100(a) Directive proposal in relation to the Open Network Provision.[188]

As announced, in May 1988 the Commission adopted Directive 88/301/EEC on Competition in the Markets in Telecommunications Terminal Equipment,[189] which declared the exclusive and special rights in relation with the import and marketing of telecommunications terminal equipment, including receive-only satellite stations incompatible with the EC Treaty. The use of the procedure foreseen in Article 86(3) EC Treaty[190], which allows the European Commission to adopt Decisions and Directives in order to put an end to an infringement of Article 86 EC Treaty, without the intervention of the Council or the European Parliament, created an important institutional conflict in the European Community. Some Member States challenged the Directive before the European Court of Justice, which upheld the Commission's position.[191]

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[187] *Ibid.* COM(88) 48 final, p. 17.

[188] *Ibid.* COM(88) 48 final, p. 23.

[189] Commission Directive 88/301/EEC, of 16 May 1988, on Competition in the Markets in Telecommunications Terminal Equipment, OJ 1988 L 131/73.

[190] Article 86 EC Treaty, and in particular its third indent, had raised some academic debate after the adoption of the Treaty. For instance, a Congress of the Ligue International contre la Concorrence Deloyale had taken place in Brussels on 5 March 1963, on the "Concurrence entre secteur public et secteur prive dans la CEE. L'article 90 du Traité de Rome. The issue was raised when the Commission adopted the first Article 90(3) Directive in 1980, Directive 80/723/EEC in relation to transparency on financial relations between Member States and public undertakings, amended through the same procedure by Directive 85/413/EEC. The Directive was challenged under the European Court of Justice which upheld the Commission's Directive, C-188/80 to C-190/80, France, Italy, UK, Ireland v. European Commission, [1982] ECR 2545.

[191] "Article 90(3) of the Treaty empowers the Commission to specify in general terms the obligations arising under Article 90(1) by adopting Directives. The Commission exercises that power where, without taking into consideration the particular situation existing in the various Member States, it *defines in concrete terms the obligations imposed on them under the Treaty", C-202/88, France* v. European Commission, [1991] ECR I-1223. In the words of the Commission "Article 90(3) does not give legislative or quasi-legislative powers. The Commission has no power to create new substantive

The announced adoption by the Commission of the Services Directive was blocked by the institutional conflict raised by the Terminals Directive. The Council refused to collaborate with the Commission for the adoption of the harmonising directive on Open Network Provision that necessarily had to accompany the liberalising directive on services. It was only by the end of 1989 that a political agreement was reached between the Council and the Commission,[192] and several months later, on the very same day both Directive 90/388/EEC and Directive 90/387/EEC were adopted. Directive 90/388/EEC, on Competition in the Markets for Telecommunications Services[193] was adopted according to the Article 86(3) procedure.[194] It declared incompatible with the Treaty the exclusive and special rights granted by the Member States for the provision of telecommunications services, with the exception of basic telecommunications services such as voice telephony and telex, as well as mobile radiotelephony, paging and satellite services.[195] Directive 90/387/EEC, on the Establishment of the Internal Market for Telecommunications Services[196] was adopted through the Article 100(a) procedure and defined the basic lines in relation to network access for the provision of the liberalised services.

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obligations for Member States , or for State enterprises, under Article 90. The Commission can only specify the implications of the existing Treaty rules, and set up procedures for making sure that existing obligations on Member States are complied with", European Commission's XXIV Report on Competition Policy (1994), point 215.

[192] An overall compromise was reached, according to which the Council would un-block the Open Network Provision Directive and the Commission would colaborate closer with the Member States in the adoption of the Article 86(3) Directives, see Press Release 10479/89 on the 1375th Council meeting on telecommunications, held in Brussels on 7 December 1989.

[193] Commission Directive 90/388/EEC, of 28 June 1990, on Competition in the Markets for Telecommunications Services, OJ 1990 L 192/10.

[194] Once again, the Directive was challenged before the European Court of Justice, and this institution upheld the Commission position, C-271/90, C-281/90 and C-289/90, *Spain, Belgium, Italy v. European Commission*, [1992] ECR I.5833.

[195] *Ibid.* Directive 90/388/EEC, Article 1(1) and Article 2(1).

[196] Council Directive 90/387/EEC, of 28 June 1990, on the Establishment of the Internal Market for Telecommunications Services through the Implementation of the Open Network Provision (ONP), OJ 1990 L 192/1.

62. De-monopolisation of mobile and satellite communications. The Commission excluded mobile radiotelephony, paging and satellite services from Directive 90/388/EEC because it was considered that these services required a special regime. Therefore, specific consultation procedures were undertaken before liberalising such services.

In 1990 the Commission published the Green Paper on Satellite Communications,[197] and proposed the full liberalisation of the earth segment, including receive only equipment, transmit/receive terminals and hub stations, unrestricted access to space segment capacity, subject to an equitable licensing procedure. The Council approved such principles,[198] and both the Terminal Directive and the Services Directive were amended in order to include satellite terminal equipment and services by Directive 94/46/EC,[199] adopted according to the Article 86(3) procedure.

The consultation procedure on the field of mobile communications was opened in 1994 with the publication of the Green Paper on Mobile and Personal Communications.[200] The Commission provided an analysis of the sector, and proposed the abolition of the remaining exclusive and special rights related to such activities, as well as the removal of all the restrictions related to the development of networks and interconnection for the provision of such services.. The Council expressed its agreement with the Commission

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[197] COM(90) 490 final, Towards Europe-wide Systems and Services. Green Paper on a Common Approach in the Field of Satellite Communications in the European Community, Brussels, 20 November 1990.

[198] Council Resolution of 19 December 1991, on the Development of the Common Market for Satellite Communications Services and Equipment, OJ 1992 C 8/1.

[199] Commission Directive 94/46/EC, of 13 October 1994, amending Directive 88/301/EEC and Directive 90/388/EEC in particular with Regard to Satellite Communications, OJ 1994 L 268/15.

[200] COM(94) 145 final, Towards the Personal Communications Environment. Green Paper on a Common Approach in the Field of Mobile and personal Communications in the European Union, Brussels, 27 April 1994.

proposal,[201] and the Commission adopted Directive 96/2/EC,[202] a new Article 86(3) Directive which amended Directive 90/388/EEC, including mobile services among the liberalised services and fixing some basic rules on licensing, spectrum management, infrastructures and interconnection.

63. The second de-monopolisation wave (1992-1998). Article 10 of Directive 90/388/EEC foresaw an overall assessment of the situation in the telecommunications sector by 1992, in order to evaluate the effect of the liberalisation of value-added services. The result was the 1992 Review,[203] in which the Commission concluded that "the lack of trans-european structures and the special and exclusive rights in substantial parts of the Community have led to a situation where major bottlenecks to telecommunications development in the Community continue to exist".[204] The Commission resumed the policy options in four scenarios. Firstly, the liberalisation process could be frozen and the *status quo* maintained. Secondly, bottlenecks could be overcome through the introduction of extensive regulation on tariffs and investments. Thirdly, the Commission proposed the option of liberalising all voice telephony services. Lastly, a partial liberalisation of voice telephony, including only international services was proposed.

After public consultation the Commission made public that "there is a broad consensus about the inevitability of full liberalisation (Option 3, which includes Option 4) before the end of the decade [...] providing special arrangements and additional transitional periods for peripheral regions and

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[201] Council Resolution of 29 June 1995, on the further development of mobile and personal communications in the European Union, OJ 1995 C 188/3.

[202] Commission Directive 96/2/EC, of 16 January 1996, Amending Directive 90/388/EEC with Regard to Mobile and personal Communications, OJ 1996 L 20/59.

[203] SEC(92) 1048 final, The 1992 Review of the Situation in the Telecommunications Service Sector, Brusels, 21 October 1992.

[204] *Ibid.* SEC(92) final, p. 18.

smaller networks".[205] As a consequence, the Commission proposed the date of 1 January 1998 for the liberalisation of voice telephony services, with an up to five years derogation for some Member States. The Council expressed its support for the liberalisation of voice telephony services before this date.[206]

By 1993, the only exclusive rights that had not been challenged by the Commission were the ones related to the telecommunications infrastructures, the hard-core of the national monopolies. The Commission considered that particularly strong political support would be necessary for the abolition of such rights. The regular strategy employed in the past of launching a public consultation in order to get the support of the actors interested in the liberalisation (the equipment industry, potential new entrants, business users, etc.), in order to force the Council to accept an Article 90(3) Directive, was considered insufficient. The Commission inserted the new liberalising objective in the framework of the new political priority after the completion of the Single market in 1992: competitiveness and employment.[207] The Commission managed to link the full liberalisation of the telecommunications sector to the political agenda of the European Council, which adopted in 1994 the principles of the highly ideological 'Bangemann Report' which recommended Member States "to accelerate the ongoing process of liberalisation of the telecom sector by opening up to competition infrastructures and services still in the monopoly area".[208]

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[205] COM(93) 159 final, Communication to the Council and the European Parliament on the Consultation on the Review of the Situation in the Telecommunications Services Sector, Brussels, 28 April 1993, p. 33.

[206] Council Resolution of 22 July 1993, on the Review of the Situation in the Telecommunications Sector and the Need for Further Development in that Market, OJ 1993 C 213/1.

[207] The European Council in Copenhagen in June 1993 invited the commission to defines a medium term strategy for growth and employment, and as a result, the Commission published COM(93) 700, White Paper on Growth, Competitiveness and Employment: the Challenges and Ways Forward into the 21st Century, Brussels, 5 December 1993.

[208] Europe and the Global Information society. Recommendations to the European Council, Brussels, 26 May 1994, p. 7.

Once the political support for the full liberalisation was achieved, the Commission published the Green Paper on the Liberalisation of Telecommunications Infrastructure,[209] which proposed the full liberalisation of the telecommunications sector, including all services and infrastructures for 1 January 1998. The Council accepted the principles and the timetable,[210] and the Commission adopted firstly an Article 86(3) Directive for the early liberalisation of alternative infrastructures (Directive 95/51/EC[211]), and finally Directive 96/19/EC, the Full Competition Directive.[212]

64. From de-monopolisation to effective competition. The process of reform of the European telecommunications sector was not completed with the privatisation of the public operators and the de-monopolisation of the markets. Due to the powerful dominance by the incumbents, it has been considered necessary to introduce different transitional mechanisms for the promotion of effective competition in the telecommunications markets. Most of these mechanisms have been defined at a Community level through harmonising directives adopted through the Article 100a procedure. In this respect, of particular interest are the Licensing Directive 97/13/EC,[213] the Interconnection

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[209] The first part of the Green Paper, fixing the liberalisation schedules, was published by the end of 1994, COM(94) 440 final, Green Paper on the Liberalisation of telecommunications Infrastructure and Cable Television Networks. Part I: Principles and Timetable, Brussels, 25 October 1994. The second part, with the reflection on the effects of such measure, was published in 1995, COM(94) 682, Green Paper on the Liberalisation of telecommunications Infrastructure and Cable Television Networks. Part II: A Common Approach to the Provision of Infrastructure for Telecommunications in the European Union, Brussels, 25 January 1995.

[210] Council Resolution of 22 December 1994, on the Principles and Time-table for the Liberalisation of Telecommunications Infrastructures, OJ 1994 C 379/4.

[211] Commission Directive 95/51/EC, of 18 October 1995, Amending Directive 90/388/EEC with Regard to the Abolition of the Restrictions on the Use of Cable Television Networks for the Provision of Already Liberalised Telecommunications Services, OJ 1995 L 256/49.

[212] Commission Directive 96/19/EC, of 13 March 1996, amending Directive 90/388/EEC with Regard to the Implementation of Full Competition in Telecommunications markets, OJ 1996 L 74/13.

[213] Directive 97/13/EC, of the European Parliament and the Council, of 10 April 1997, on a Common Framework for General Authorisation and Individual Licenses in the Field of Telecommunications Services, OJ 1997 L 117/15.

Directive 97/33/EC,[214] and the Voice Telephony Directive 98/10/EC.[215] The process of reform of the European telecommunications sector will only be completed once effective competition rules the provision of telecommunications services in all the Member States.[216]

3.5. CONCLUSIONS.

65. Final. By the end of 19th century a well-established tradition of direct public intervention existed in most of continental Europe. Early medieval precedents, strengthened by absolute monarchies and reshaped by liberal revolutions led to the monopolisation by the public authorities of the network industries which appeared during the industrial revolution. This was the case of telecommunications.

The telegraphy and telephony markets were nationalised not because of their natural monopoly structure or for the protection of user's rights. These activities were monopolised by the State as a result of their relevance for public security and economic activity in general. It was considered a risk to leave the management of such a relevant activity to private entities.

Technological development, the inefficiency of the public monopolies, the pressure of entities such as the European Union, the influence of conservative political ideals and the example of the US challenged the very same existence of the telecommunications public monopolies.

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[214] Directive 97/33/EC, of the European Parliament and the Council, of 30 June 1997, on Interconnection in Telecommunications with Regard to Ensuring Universal Service and Interoperability through Application of the Principles of the Open Network Provision (ONP), OJ 1997 L 199/32.

[215] Directive 98/10/EC, of the European Parliament and the Council, of 26 February 1998, on the Application of Open Network Provision (ONP) to Voice Telephony and on Universal Service for Telecommunications in a Competitive Environment, OJ 1998, L 101/24.

[216] See SCOTT, C. (1996): "Current Issues in EC Telecommunications Law", in *The Future of EC Telecommunications Law*, Bundesanzeiger, Köln, pp. 21-40.

The reform faced important obstacles. The elimination of the monopolies not only affected different interests (trade unions, *elites* in control of the monopolies etc.). It even required a major transformation of the model of public intervention in the economic activity.

The elimination of public monopolies required the introduction of new indirect instruments of intervention, new mechanisms, and even new institutions.

PART II

INTERVENTION IN LIBERALISED MARKETS

CHAPTER 4

A NEW MODEL OF PUBLIC INTERVENTION IN EUROPE.

SUMMARY: 4.1. The Need of Public Intervention. 4.2. Instruments of Public Intervention. 4.3. The New Morel: Transplant or Convergence? 4.4. Conclusions.

4.1. THE NEED OF PUBLIC INTERVENTION.

66. The process of liberalisation. As it was described in Chapter 3,[217] in the early 90s the decision to fully eliminate public national monopolies in the European telecommunications markets was adopted. De-monopolisation was the initial measure of a profound reform of the sector that would substitute the direct provision of the telecommunications services by the public authorities with the provision of such services by private operators.

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[217] *Vide supra* Chapter 3. Nationalisation and Liberalisation of European Telecoms Markets.

Consumer satisfaction would no longer be pursued through the direct intervention by the public authorities, but through the mechanisms of supply and demand in a competitive market. The process of liberalisation, thus, can be understood as the substitution of the guarantee of the direct presence of the State by the discipline imposed on private operators by competition in the market, but always with consumer welfare as an objective.

Effective competition became at that stage the fundamental requirement for the success of the process of reforming the sector. If the traditional intervention of the State would not be substituted by the discipline imposed by effective competition, operators would have no incentive to meet the users' demands and their welfare would, therefore, not be ensured. The lack of effective competition would entail the failure of the whole process of reform of the telecommunications sector.

67. De-monopolisation and the general interest. De-monopolisation has been the initial measure of the process of reform of the European telecommunications markets. De-monopolisation has usually been accompanied by the privatisation of the assets that were in hands of the national authorities, even if such process a has not been imposed by the European institutions.[218]

Nevertheless, it has been widely accepted that the process of liberalisation does not finish with de-monopolisation and privatisation. On the contrary, the elimination of the exclusive rights is only the first step, the simplest step, in the process of the transformation of the telecommunications sector, from a public driven activity to a competition driven one. The process of reform of the

[218] Privatisation was often considered a parallel element to de-monopolisation in the process of liberalisation. In the new environment, competition was supposed to drive the sector, and public ownership would not only obstruct the emergence of competition but also would not ensure a powerful instrument for the public authorities as no discrimination in favour of the public operator would be accepted. Nevertheless, a significant amount of Member States have not completely privatised the public operator (including France and Germany).

European telecommunications markets will work if and only if public monopolies are replaced by effective competition.[219]

68. Obstacles to competition. The transition from national public monopolies to effective competition, nevertheless, faced some obstacles which could obstruct or at least complicate the emergence of the necessary discipline of the telecommunications markets.

Some of those obstacles derived from the abusive behaviour of the former monopolists. The long-lasting exclusive rights enjoyed by the incumbents ensured an almost absolute dominance of the telecommunications markets for the former monopolists. They could abuse such market power and develop practices which exclude new comers from the telecommunications markets. Practices such as refusals to deal, predatory pricing, exclusionary discriminations or tying can create significant barriers to entry and even exclude new operators from the market.

Nevertheless, the structure of some segments of the market, together with the very same presence of the former monopolists constituted the most significant obstacle in the telecommunications markets. The character of network industry introduces an element of differentiation in the telecommunication industries and other public utilities. On the one hand, the well-known network externality effect obstacled the development of new networks, as the value of a network for a user is directly related to the extension of its coverage. On the other hand, network industries present significant economies of scale and scope.

The control by the former monopolist over the only existing universal public telecommunications network allowed him to benefit from the economies

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[219] This view is widely shared. See for instance BAER, W. (1997): "*The Role of the Competition Agency in Regulatory Reform*", OECD, Paris, p. 22.

of scale and scope and from the network externality effect. In market segments where such benefits are relevant, only in the case new comers can share these benefits with the incumbent, unless for a transitional period, there will be a chance for effective competition to emerge.

Public monopolies could not be substituted by "ruthless, Darwinian, free-market competition that doesn't require the regulators to do anything but attend the funerals".[220] The main reason is that such funerals would probably be organised for the new comers trying to access a market characterised by the high barriers to entry, originated, among other reasons, by the high sunk costs for the construction of alternative networks, the significant economies of scale and the network externality effect. Furthermore, the lack of competition would allow the private monopolist to impose abusive conditions for the obtention of monopoly rents, what would lead at the long run, to the funeral of the very same public authorities who did not conclude the process of transition to effective competition.

69. Universal service. At the same time, the most important argument of the forces opposing the elimination of the exclusive rights in the telecommunications markets was that the introduction of competition in such sector would put an end to the cross-subsidies between different market segments. Such cross-subsidies allowed the provision of those services considered of particular relevance, at a price under cost, as well as the provision of all services in all the national territory at the same price, independently of the higher costs of the provision in particular areas such as rural or scarcely populated areas. It was obvious that the elimination of exclusive rights would allow new comers to profit from the unbalanced price structure through the exploitation of those services provided by the incumbent

[220] Position maintained in the US by Representative E. J. Markey, see PIRAINO, T. (1997): "A Proposed Antitrust Analysis of Telecommunications Joint Ventures", in *Wisconsin Law Review*, vol. 1997, no. 4, pp. 639-704.

at a price clearly above cost in order to finance other services, "screaming" the market. As a result, the incumbent would have to face such competition through the re-balancing of tariffs, adjusting prices to costs, and through the elimination of the provision of non-profitable services, such in the case of rural and isolated areas, or low-usage clients.

Most of the defendants of the liberalisation process argued that competition would enhance efficiency and therefore a reduction of costs and a reduction of prices. Nevertheless, it was clear that network competition would take years to develop and during such a period, the former monopolists might be tempted to obtain some monopoly rents in those market segments firmly controlled, which necessarily coincide with the market which already have suffered price increases due to the process of re-balancing.

At the same time, it was evident that competition, even promoting efficiency, would never be able to ensure the provision of telecommunications services under cost, as was traditionally the case for high-cost areas and low-use clients. Even with the reduction of costs attributed to the introduction of competition, the affordability of the telecommunications services for all the citizens would not automatically be ensured by the de-monopolisation of the sector, or even by effective competition in the sector.

70. Options. Different policies could be considered in order to overcome the obstacles for the emergence of effective competition. The States involved in a process of liberalisation of the telecommunications markets could rely on market forces to overcome them, divest the monopolist in order to reduce its market power, or introduce behavioural mechanisms directed to reduce obstacles to competition.

Firstly, public authorities could consider that existing barriers to entry did not impede the emergence of competition in the telecommunications markets and to leave to market forces the development of the most effective solutions to

overcome them. As a matter of fact, it was claimed that technological progress had not only eliminated the natural monopoly character of the market but also most of the traditional barriers to entry, as new technologies could provide more efficient network solution than those traditionally implemented by the incumbent. As a result, new comers could be in an even better position than the incumbents, as they would not suffer dead weights as an obsolete network, an excessive expensive working force or even a brand associated to inefficiency. The existing mechanisms provided by the existing rules on competition would be enough to prevent the conventional exclusionary practices implemented by the incumbent, just as in any other economic sector.

This was the option adopted in some of the leading experiences of liberalisation, particularly in New Zealand. In this country the process of reform was limited to the elimination of the exclusive right traditionally enjoyed by the incumbent. For the rest, no specific mechanism of public intervention was foreseen, and only the regular mechanisms envisaged by the local rules on competition were at the disposal of the new comers in order to defend their interest against the potential anticompetitive actions of the former monopolists.

Secondly, public authorities could consider the possibility to reduce the market power of the incumbent through a structural intervention, that is, through the divestiture of the former monopolist. In such a way, the asymmetric structure of the market could be eliminated. Such an intervention would diminish the potential risks derived from the vertical integration of the incumbent, particularly the risk of blocking the emergence of competition in the more dynamic service markets through the exercise of market power in the infrastructures markets. This strategy was followed in the US at the beginning

of the 1980s, with the divestiture of the Bell System,[221] and at a latter stage in Japan.[222]

This option was never seriously consider in Europe due to the relatively small size of the European operators in relation to their American and Japanese counterparts. The divestiture of all the European operators would have extremely fragmented the European market, and would have favoured entrance in the market of the financially more solid American operators. Furthermore, the elimination of the vertical integration, even if would have eliminated the risk of extension of market distortions, would have not eliminated the existing failures in some market segments.

The final option was to develop a framework for public intervention for the promotion of competition in the liberalised sectors which, based in the respect for the position of the former monopolist, would introduce mechanisms to reduce the obstacles to competition. This was the option finally adopted in Europe, as well as in most of the States involved in a liberalising process.

71. The European strategy. There was widespread consensus in Europe about the need not to eliminate public intervention in the telecommunications sector but to replace national public monopolies with new instruments in grade to make possible the promotion of competition and the satisfaction of the general interest.

On the one hand, it was considered that public intervention was necessary in order to promote the emergence of effective competition in the telecommunications markets. Barriers to entry to the telecommunications markets, and particularly to the network segments, are of particular relevance. Network markets are characterised by the existence of important economies of

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[221] *Vide supra* Chapter 2.4.3. Deregulation of the US Telecoms Markets (1969-2000).

scale as well as by the predominance of sunk costs. These facts, together with the dominant presence of the former monopolists, make entry into the network markets particularly complicated.

Public intervention can promote and facilitate market entrance as well as the development of effective competition not only in the services markets (what was facilitated by the unbalanced tariff structure) and in the network markets, and objective hitherto indispensable for the creation of a competitive environment in the sector. Nevertheless, it has to be taken into account that the emergence of effective competition is not dependent upon a mere political decision, as was the case with de-monopolisation. It is for the undertakings to enter the market and offer an alternative to the incumbent. Public authorities can promote such actions, but cannot impose them.

On the other hand, despite the political option in favour of competition as the driving mechanism for the telecommunications sector as the best model to promote the satisfaction of the general interest in the sector, it was considered that in some cases immediate public intervention would be necessary in order to defend immediately the general interest.

Firstly, in the period of transition from monopoly to competition, the incumbents would be free from competitive constraints in significant market segments as relevant as the local loop. In order to obstruct the exploitation of such market power against consumers, public action was considered to be necessary. Furthermore, due to the very same structure of some telecommunication markets, monopoly could be substituted by a collusive oligopoly in which effective competition would be missing.

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[222] See TANAKA, E. (1997): "The Status of Nippon Telegraph and Telephone Corporation (NTT)", in *Telecommunications Policy*, vol. 21, no. 2, pp. 85-99.

Secondly, there are general interest objectives that are out of the scope of the market, as they are not necessarily among the results of competition. The provision of services below costs in order to ensure the affordability of the services considered indispensable for the participation in a democratic society, for instance, cannot be ensured by the market even once effective competition emerges. It is for these reasons that immediate public intervention is considered necessary for the protection of the general interest.

4.2. INSTRUMENTS OF PUBLIC INTERVENTION.

4.2.1. Instrument for Indirect Intervention.

72. Instruments. Even if it was widely belived that public intervention was necessary in order to complement the market mechanisms, particularly in the period of transition to competition, the elimination of the traditional mechanism of public intervention in the telecommunications markets (the public monopoly) required the implementation of new mechanisms that would allow the indirect intervention of public authorities.

Competition Law appeared as the first instrument of public intervention in a de-monopolised environment. Community competition Law had plaid a decisive role in the de-monopolisation, and provided mechanisms for the control of market power, the main issue after the elimination of the legal monopolies.

Nevertheless, the rules on competition face some limitations. On the one hand, no particular mechanism is envisaged for dominant positions originated by a exclusive right considered incompatible with the EC Treaty, and as a result the general regime defined in Article 82 EC Treaty has to be applied. This regime is based on the respect to the dominant position obtained through growth in the market thanks to efficiency, and the imposition of behavioural

limitations in order to avoid abuses directed to the exploitation of dominance in respect to consumers, and to avoid exclusionary practices devoted to the maintenance of the dominance or even its increase.

On the other hand, European competition authorities, particularly at a Community level, did not have the resources to closely monitor the market during the exceptional period of transition from monopoly to competition . At the same time, antitrust procedures are long and cumbersome, and did not seem fitted to solve the issues arisen due to the reform of the sector timely and in an efficient way.

The European tradition of direct intervention in the economic activity has produced an underdevelopment of the instruments of indirect intervention. The American model of regulatory intervention has provided some useful insights about the possible mechanisms of intervention as well as about the risks of such mechanisms. Nevertheless, the attention to the American regulatory model does not mean an automatic transplant of such a model, but rather an adaptation of some of the regulatory mechanisms to the administrative traditions of the different Member States.

The European authorities have designed a model of asymmetric, sector specific regulation, characterised by the national authorities imposing specific legal obligations on the operators according to their position in the market in order to protect the general interest. The obligations generally defined by the Community and national Legislators are specified for each operator. This is a very flexible instrument that allows public authorities to facilitate market access to new comers as well as their development, at the same time that the specific treatment of market dominance allows for the obstruction of exploitative behaviours contrary to consumers' interests and to profit from the dominant situation in order to ensure the universality of certain services.

4.2.2. Competition Law.

73. Nature. Competition Law was only adopted in Europe after World War II.[223] The European Economic Community Treaty defined as a fundamental principle of the new entity, the necessity to defend and promote competition in the European Common Market, and adopted substantive provisions which declared as incompatible with the Treaty the adoption of restrictive agreements, the abuse of dominant positions, and certain State aids. Even if some European countries adopted laws on competition before the adoption of the EEC Treaty, it was only at a latter stage, and as a consequence of the influence of the EC, that all the Member States enacted laws on competition, usually following closely the Community model.[224]

Competition Law,[225] both at a Community and at a national level, is applied to most economic activities, in such a way that no particular rules exist for the telecommunications sector. Competition Law is, therefore, a horizontal instrument of intervention.

The rules on competition provide an instrument of indirect intervention for the protection of the general interest. Firstly, it is an indirect intervention in the sense that public authorities do not intervene directly for the satisfaction of the general interest through the provision of a good or a service, but through the imposition of legal obligations on the actors active in the market.

Secondly, the intervention is indirect in the sense that the rules on competition do not immediately protect the interest of consumers, but rather

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[223] *Vide supra* Chapter 3.2. Competition Law in Europe.

[224] See LAUDATI, L. (1998): "Impact of Community Competition Law on Member States Competition Law", in *Competition Policies in Europe*, edited by S. Martin, Elsevier, Amsterdam, pp. 381-410.

[225] For an overview of Community Competition Law see, for instance, BELLAMY and CHILD (1993): "*Common Market Law of Competition*", Sweet and Maxwell, London, and KORAH, Valentine (1994): "*An Introductory Guide to E.C. Competition Law and Practice*", Sweet & Maxwell, London.

protect the structure that makes possible the satisfaction of such interest. The purpose of the rules on competition is to protect competition.[226] The basic assumption underlining this set of rules is that competition imposes an effective pressure on companies to improve their products and lower their costs. In any case, these rules do not protect competition for competition's sake. The ultimate objective is to ensure that consumers benefit from the lower costs in the form of low prices and from the development of new products fitted for their needs.

The main mechanism of intervention is the prohibition, in abstract, of certain behaviours that might affect the competitive process and reduce competition in the market, in such a way that the constraints imposed on competition would disappear and companies would be able to maximise their benefits at the expenses of consumers. The fundamental feature of the rules on competition is their proscriptive character, as they prohibit certain behaviours rather than impose positive obligations on economic entities.

Competition authorities can intervene both *ex post* (in order to obstruct collusion and abuses of dominance) and *ex ante* (mergers), but in both cases evaluate the effects towards the future of the pertinent behaviour in the relevant market.

74. Competition Law and de-monopolisation. The most decisive application of the rules on competition in the telecommunications sector took place when the Commission, upheld by the Court, adopted the Article 86(3) (former Article 90) Directives[227] which declared contrary to Article 82 (former Article 86) EC Treaty (among other provisions of the Treaty) the exclusive

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[226] See EHLERMANN, C. D. and LAUDATI. L. ED. (1998): "*European Competition Law Annual 1997. Objectives of Competition Law*", Hart.

[227] *Vide supra* Chapter 3.4.3. Liberalisation of the Telecoms Markets (1987-1998). For a in-depth analysis see LAROUCHE, P. (2000): "*Competition law and Regulation in European telecommunications*", Hart, Oxford, pp. 37-111.

rights granted in relation to telecommunications terminal equipment[228] and telecommunications services.[229] According to the Community institutions, "exclusive rights granted for the provision of telecommunications services are also incompatible with Article 90(1) of the Treaty, in conjunction with Article 86 [...] since their grant amounts to the reinforcement or the extension of a dominant position or necessarily leads to other abuses of such position".[230]

At the same time, the regular application of Community competition Law has also been used by the Commission to foster the liberalisation of the sector. It is commonly accepted, for instance, that the agreement of Germany to the approval of Directive 95/51/EC, the Alternative Infrastructures Directive, was facilitated by the threat of the Commission to block the Atlas joint venture (fundamental for the international strategy of the German national champion, DT). In the same way, the acceleration of the de-monopolisation of the sector in Spain was facilitated by the threat of the Commission to block the participation of Telefónica in Unisource.[231]

The relevance of the rules on competition in the European liberalisation process should not be misunderstood. The action of the Commission was based on Article 86(3) of the EC Treaty. This provision is more related to the

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[228] "The exclusive right to import and market terminal equipment must therefore be regarded as incompatible with article 86 in conjunction with article 3, and the grant or maintenance of such rights by a Member State is prohibited under Article 90(1)", Commission Directive 88/301/EEC, of 16 May 1988, on competition in the markets in telecommunications terminal equipment, OJ 1988 L 131/73, recital 13. The ECJ upheld the use of the Article 90(3) procedure, "Article 90(3) of the Treaty empowers the Commission to specify in general terms, by adopting directives, the obligations imposed on the Member States by Article 90(1) as regards public undertakings and undertakings to which they have granted special or exclusive rights", C-202/88, *France v. Commission*, [1991] ECR I-1223, paragraph 1.

[229] "The exclusive rights to telecommunications services granted to public undertakings or undertakings to which Member States have granted special or exclusive rights for the provision of the network are incompatible with article 90(1) in conjunction with Article 86", Commission Directive 90/388/EEC, of 28 June 1990, on competition in the markets for telecommunications services, OJ 1990 L 192/10, paragraph 17.

[230] Commission Directive 96/19/EC, of 13 march 1996, amending Directive 90/388/EEC with regard to the implementation of full competition in telecommunications markets, OJ 1996 L 74/13.

[231] *Vide* LAROUCHE (2000) (*supra* footnote 227).

effectivity of the Community legal framework that to the antitrust rules themselves. Therefore, the role of the rules on competition as a mechanism to open markets should not be over emphasised. As an example, even if antitrust played an important role in the deregulation of the US market, it was the Legislator, together with the FCC, who finally completed the reform of the market.

75. Competition Law after de-monopolisation. If Community competition Law played an important role in the de-monopolisation of the European telecommunications markets, even more important is the role of both Community and national rules on competition once the exclusive rights on the sector have been eliminated.

The Commission has already adopted a significant number of Decisions applying competition Law to the telecommunications sector.[232] Collusive practices such as market sharing and price fixing are particularly likely in the telecommunications markets due to their oligopolistic tendency. Market sharing is favoured, on the one hand by the traditional existence of national monopolies, which, after de-monopolisation might be tempted to collude among them in order to mutually agree the exclusion of entrance in each other's traditional geographic markets. On the other hand, market sharing is probable in respect of product markets. Price fixing is also a risk in an oligopolistic market, where price wars might, in the long run, damage all competitors.[233]

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[232] See TEMPLE LANG, J. (1997): "*Media, Multimedia and European Community Antitrust Law*", 24th Antitrust Conference of the Fordham Corporate Law Institute, and MONTERO PACUAL, J. J. and SOUTO SOUBRIER, L. (1998): "De la desmonopolización a la competencia efectiva. Aplicación de la normativa antitrust comunitaria y española en el sector de las telecomunicaciones", in *Boletín Latinoamericano de Competencia*, no. 4, pp. 83-104.

[233] The Commission already observed the existence of price fixing agreements in the framework of the CEPT, see XX Report on Competition Policy, 1990, paragraphs 56 and 57.

Particularly important have been the Decisions in relation to strategic alliances. The Commission has adopted a positive position towards strategic alliances if they are created in order to provide global services,[234] in order to create alternative providers,[235] or in order to develop new services if important investments with significant risks are involved.[236] On the contrary, the Commission has adopted a negative position if the strategic alliance (particularly if it is concentrative) has the objective of reinforcing the position of the incumbent operators in their geographical markets, through the extension of their position to neighbouring markets, or through the control of bottlenecks.[237]

4.2.3 Economic Regulation.

76. A new model of public intervention in Europe. The process of the reform of the telecommunications sector in Europe has eliminated the traditional instrument of public intervention, the public monopoly. It has been proven that the rules on competition, even if they have an important role to play in the sector, face decisive limitations. A different instrument of intervention was needed in order to govern the transition from monopoly to competition.

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[234] Such was the case of *BT/MCI*, *Global One*, or *Unisource*, see as an example Commission Decision 96/546/EC, of 17 July 1996, *Atlas*, OJ 1996 L 239/23.

[235] The Commission has generally accepted horizontal concentrative agreements for the creation of alternative operators or for the entrance of operators active in other geographical markets in new markets. As an example, Commission Decision 94/922/EC, of 9 November 1997, *Ameritech/Tele Danmark*, OJ 1998 L 25/18. The same position has been adopted by the Commission in respect to vertical concentrative operations for the creation of alternative operators to the incumbent.

[236] An example of this approach was the Commission Decision 97/39/EC, of 18 December 1996, *Iridium*, OJ 1997 L 16/87, where the Commission considered that the co-operative joint venture for the creation of a global network of low-orbit satellites for the provision of universal mobile communications was not even contrary to article 85.1 EC Treaty.

[237] Commission Decision 96/117/EC, of 19 July 1996, *Nordic Satellite Distribution*, OJ 1996 L 53/20, paragraph 164. The best example of this policy was the Commission Decision 94/922/CE, of 9 November 1994, *MSG Media Service*, OJ 1994 L 362/1, where the Commission blocked a concentrative joint venture between Deutsche Telekom, Bertelsmann and Kirsch in order to create a platform for the provision of digital television.

The model adopted by the European authorities has been the so-called economic regulation.[238] Economic regulation, can be defined as the continuous and concentrated control of the market by public authorities through the imposition of legal obligations on the private operators, according to their position in the market, in adaptation of the abstract obligations defined by the Legislator, with the objective to ensure the adaptation of the functioning of the markets to the general interest objectives.[239]

Economic regulation is a public intervention instrument of an indirect nature since public authorities do not directly provide any product or service to the citizens, but merely impose obligations on private actors in order to guarantee that they satisfy the needs of the citizens.

Economic regulation can be adapted to very different situations and can be used for the implementation of very different policies, as the American experience proves.[240] Regulatory mechanisms have been established in Europe after the de-monopolisation of the markets in order to complete the liberalisation process, promoting the emergence of competition and ensuring the immediate protection of the general interest. This regulatory intervention is far away from the American price-and-entry regulatory experience, which obstructed competition, and is closer to the more recent American regulatory

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[238] Studies on economic regulation are quite numerous in the US as well as in the UK. In continentak Europe its is of great interest the study of ARIÑO, G. (1993): "*Economía y Estado*", Marcial Pons, Madrid; and MARTÍNEZ LÓPEZ-MUÑIZ (1997): "La nueva regulación económica en España", en "*El nuevo servicio público*", Marcial Pons, Madrid, pp. 185-269. French doctrine has not paid particular attention to this new phenomenum, but some points have been raised in CHEVALIER, J. (1995): "Les autorités administratives indépendentes et la régulation des marches", in *Justices*, no. 1, pp. 81-90.

[239] In a broad sense, competition Law could be considered an example of economic regulation. In this pages, nevertheless, we distinguised it from the sector specific regulation which is being developed in Europe. The reason is that competition Law is a very precise mechanisms of regulation, as only very specific obligations are imposed on market players and, furthermore, such obligations are mostly of a negative nature, that is prohibitions. Economic regulation is very broad and comprises negative as well as positive obligations.

models after the process of de-regulation. In the European model, regulation complements and promotes competition.

Economic regulation is flexible in relation to the purposes of the intervention. Regulatory obligations may have the purpose of ensuring the effectivity of the constraints imposed by competition, but can go further, and promote the emergence of competition,[241] or introduce obligations with the purpose of the immediate protection of the general interest.

Regulation is also flexible in relation to the mechanisms and timing of intervention. Regulation is implemented through the definition of obligations imposed on the operators in the market. Such obligations can be of a proscriptive nature, but also of a prescriptive one. At the same time, regulatory obligations adapting the abstract legal obligations to the specific situation of an undertaking can be imposed by *ex ante*, in order to introduce legal certainty, but can also be imposed when a conflict arises, or when the situation in the market is modified.

As a consequence, economic regulation is a good complement to the rules on competition. Regulation is broader in its scope. While the rules on competition protect a very focused interest (the competitive character of the market), economic regulation can be used to protect a wider ambit of interests. Regulation can be adapted to a specific market, while the rules on competition are horizontally applied. Regulatory obligations are broader as not only can proscribe, but also prescribe behaviours. Finally, regulatory obligations can be imposed *ex ante* or *ex post*.

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[240] For an overview of the most representative regulatory models in the US, the price-and-entry regulation, social regulation etc., *vide supra* Chapter 2.1. Origins and Evolution of Economic Regulation.

[241] See some reflections in HANCHER, L. (1990): "*Regulating for Competition. Government, Law and the Pharmaceutical Industry in the UK and France*", Claredon Press, Oxford.

It is clear that regulation provides a broad range of intervention mechanisms, and this is precisely its main risk. This kind of intervention can lead to arbitraness and over-regulation.

77. Regulatory mechanisms. In order for regulation to be successful, effective mechanisms for the imposition of obligations on the operators have to be defined. The American experience provides useful information on the benefits and risks of different mechanisms. But in any case, such mechanisms have to be adapted to the European administrative experience, and more particularly to the administrative system of each Member State.

Community directives have defined the objectives of regulatory intervention, as well as the basic lines of the administrative mechanisms that should be used to guarantee the effectiveness of the public intervention. It is for Member States to implement such principles and adapt them to their national characteristics. The framework defined by the Community authorities covers a varied number of regulatory mechanisms.

The starting point of the regulatory intervention is the definition of mechanisms devoted to ensure the flow of information from the regulated industry to the regulatory authorities. Such mechanisms are necessary in order to reduce as much as possible the information asymmetry which favours the actors active in the market against the public authorities, which can only have an indirect knowledge of the market conditions. In such a way, different obligations have been designed in order to ensure the flow of clear and precise information from the market to the regulatory authorities.[242]

The fundamental regulatory mechanism is the definition *ex ante* of obligations imposed on different categories of operators. Regulatory

[242] Just as examples can be identified the obligations in relation to cost accounting imposed by Directive 97/33/EC, and the conditions in relation to the communications of information by the operators envisaged in Directive 97/13/EC.

authorities, taking advantage of their close control on the market evolution, can adapt the basic obligations defined by the Legislator to specific categories of operators. Such intervention introduces transparency and legal certainty. Nevertheless, the exercise of quasi-normative activities by bodies such as the regulatory authorities, which often are exempted of direct control by the national Parliaments, creates problems of constitutionality in a significant number of Member States.[243]

At the same time, regulatory obligations can be imposed on specific operators. Such is the case of the imposition of conditions on the operators at the moment of the granting of the license or authorisation to access the market.[244] This kind of intervention has been particularly popular among Member States since it closely resembles the figure of the concession, one of the traditional mechanisms of *service public* intervention.

The Community authorities were fully aware that these mechanisms of intervention involved risks of foreclosure, and for these reason adopted Directive 97/13/EC, which reinforced freedom for market access as one of the leading principles of the process of reform of the sector.[245] Member States could impose conditions on operators for the granting of the title to access the market, but this condition should always be proportionate and non-discriminatory, as market access was not a right granted by the public authorities anymore, but a pre-existing right merely recognised and controlled by the public authorities.

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[243] The most representative case is the French. The most relevant decisions of the ART have to be homologated by the Ministry, in order to avoid the problems reflected in the decision of the *Conseil d'État* n 88-248 DC of 17 January 1989. See LASSERRE, B. (1997): "L'Autorité de régulation des télécommunications", in *L'Actualité Juridique-Droit Administratif*, vol. 53, no. 3, pp. 224-228.

[244] Directive 97/13/EC states that "conditions attached to authorisations are necessary in order to attain public interest objectives to the benefit of telecommunications users", paragraph 4.

[245] "General authorisations and individual licensing systems should provide for the lightest possible regulation

Regulatory authorities can also impose specific obligations on the single operators after the granting of the license to operate. This possibility is foreseen by Community Directives in relation to the resolution of conflicts between operators, in particular in interconnection and market access conflicts.[246]

Regulatory authorities solve such conflicts through the specification of the obligations imposed on each operator. Furthermore, regulatory authorities can impose specific obligations on single operators after the granting of the license and without the involvement of the operator in a specific conflict with another operator. This is the clearest case of regulatory intervention, and the one that is more distant from the administrative traditions of most of the Member States. The adaptation of the rules on the modification of the conditions of a concession title does not seem the most appropriate decision for the introduction of such possibility, as it would introduce provisions on the maintenance of the financial stability of the operator. On the contrary, most of the regulatory authorities have been assigned the possibility of adopting measures *ex post*. This mechanism should be developed, carefully, but with resolution.

78. Regulation and Administrative Law. Regulatory intervention has not only promoted the establishment of sector-specific independent authorities[247], but also requires the adaptation of the existing administrative procedures and possibly even the review of the notion of administrative act.[248]

With regards to the rules on administrative procedures, it seems necessary to strengthen the mechanisms that allow the reduction of formalisms

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[246] See in particular Directive 97/33/EC.

[247] *Vide infra* Chapter 6. Institutional Framework.

[248] We follow in these lines the research in ARIÑO ORTIZ, G. (1997): "Sobre el significado actual de la noción de servicio público y su régimen jurídico. (Hacia un nuevo modelo de regulación)", in "*El nuevo servicio público*", Marcial Pons, Madrid, pp. 49-54; and MARTÍNEZ LÓPEZ-MUÑIZ (*vide supra* footnote 238).

and therefore, the simplification of the procedure. Nevertheless, it has to be taken into account that the principle of legality should always be respected. As a result, transparency and accountability have to be guaranteed at every stage of the procedure, and the motivation of every decision of the regulator has to be complete and convincing. Existing mechanisms such as the conventional conclusion of the procedure might provide a solution for the necessary flexibility required by regulatory intervention.

With regard to the very same administrative acts, the adaptation of the content of the obligations established in the legislation to the specific position of each operator entail a substantial degree of discretionality which might challenge the traditional nature of such acts. Discretionality might be incompatible with the traditional principle of legality of the administrative act. Regulation challenges the traditional distinctions between powers in such a way that regulatory acts concentrate characteristics which seem closer to judicial acts or even to legislative acts. The lack of administrative review that characterises independent authorities, and the limited judicial review (it can only compensate damages, but it cannot restore the situation in the market) strengthen the problem. Once again, transparency and accountability seem to provide the only solution.[249]

79. Regulating telecoms. There are two characteristics of the regulatory model that make it suitable for the European situation. Firstly, the regulatory model of public intervention can be compatibilised with competition in the market, the force designed by the European authorities for the driving of the sector. The imposition of obligations on the operators active in the market does not necessarily obstruct the regular functioning of the free market mechanisms of demand and supply, in such a way that public intervention can complement

[249] See EBERLEIN, B. (1998): "*Regulating Public utilities in Europe: Mapping the Problem*", EUI Working Papers, RSC no. 98/42, Florence

the market, which has been decided to be the basic mechanism for governing the sector. However, in order for public regulatory intervention not to obstruct the competitive mechanisms, particular knowledge and attention by the public authorities is required.

Secondly, the regulatory model allows public authorities to face the problem of the strong dominance of the former monopolists, through the adaptation of the conditions defined for the provision of the telecommunications services to the specific situation of each operator. The new legislation on telecommunications defined at a Community level and implemented by the Member States allows public authorities to adapt the abstract and general obligations and conditions for the provision of services to the specific situation of each single operator, and in particular to the operators enjoying market power thanks to an exclusive right declared incompatible with the EC Treaty.[250]

The asymmetric distribution of obligations among the operators active in the market allows public authorities to face the problems raised by liberalisation, problems that cannot be efficiently managed by Competition Law. Such distribution has favoured the denomination of asymmetric regulation[251] to the regulatory model that is being implemented in Europe (which by the way, is not substantially different to the model applied in the US).

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[250] Directive 97/13/EC declares that "Member States should therefore be allowed to impose specific conditions on undertakings providing public telecommunications networks and telecommunications services by virtue of their market power", paragraph 14.

[251] See BENZONI and SVIDER (1994): "Departing from monopoly: asymmetries, competition dynamics and regulatory policy", in "*Asymmetric Deregulation. The Dynamics of Telecommunications Policy in Europe and the United States*", Noam and Pogorel eds, Ablex, Norwood; and PERRUCCI, A. and CIMATORIBUS, M. (1997): "Competition, convergence and asymmetry in telecommunications regulation", in *Telecommunications Policy*, vol. 21, no. 6, pp. 493-512.

The asymmetric distribution of obligations between the operators according to their market position can be used to promote entrance and development of new competitors and, in this way, the apparition of effective competition in the market. This is the case of the regulatory obligations in relation to network interconnection and access defined in the Community Directives, implemented by the national legislations and enforced by the national regulatory authorities.

At the same time, the special obligations imposed on operators with significant market power can be used to avoid the risk of exploitative abusive behaviour by the incumbents in the period of transition to competition, a risk which does not exist in the case of new operators, at the same time that the imposition of stricter obligation on operators with significant market power allows public authorities to take advantage, for the general interest, of the comprehensive and solid presence of the former monopolists, in order to implement general interest policies. Such is the strategy established in the Community Directives and, again, implemented by the NRAs.

4.3. THE NEW MODEL: TRANSPLANT OR CONVERGENCE?

80. Towards indirect complementative public intervention in Europe. Telecommunications reforms do not only affect market structure, but also public intervention mechanisms, both in the US and Europe. Market substitutive intervention is being eliminated, giving place to competition and a market complementative intervention of an indirect nature. That is, public authorities do not try to eliminate the market mechanisms. On the contrary, they build their intervention on such mechanisms not through their participation in the market, but through the imposition of legal obligations on the private actors active in the liberalised market.

This reform is simpler in the US where there is a long tradition of indirect intervention in the economic activity. It does not mean that no reform has been undertaken in the US. It is obvious that the telecoms sector has suffered a major evolution. Nevertheless, such evolution has focused on the transition from market substitutive intervention, that is, public intervention devoted to impose on the monopolist the pressures suffered by a company in a perfectly competitive market, to effective competition.

The point is that such a reform has not required the creation of new institutions nor the implementation of new instruments for regulatory intervention. The FCC and the state PUCs, together with traditional antitrust authorities, no matter how controversial, conform a institutional framework in grade to face the challenges of the new market structure. Along the same lines, the traditional regulatory mechanisms, such as licensing, the imposition of legal obligations to the actors on the market, etc., can be used to implement the new policies.

In Europe, on the contrary, the reform is more complicated, because the same problems of elimination of monopolies and promotion of competition are faced but, in addition, direct intervention has to be substituted by indirect mechanisms, which require the creation of institutions and new legal instruments.

The reform of the public intervention instruments, institutions and mechanisms in the telecommunications sector might be a step in the process of convergence of the two approaches we have differentiated with regard to public intervention in defence of the general interest.

On the one hand, the increasing complexity of modern society is strengthening the tendency to create specific frameworks for the protection of specific public interests. A general tendency in Europe to "unbundle" the different public interest in order to create specific institutions for the evaluation

of the different general interests has been identified. If a specific framework is created for the protection of a public interest, the risk of such interest being dismissed as a result of political interference between different and conflicting interests is reduced. The examples of public intervention for the protection of workers and for the ruling of urban expansion demonstrate that this is an "indigenous" tendency that cannot be directly linked to an American influence.[252]

The continuous technological progress has multiplied the products and services offered in the market, the options available for consumers. At the same time, the economic structure of the market is increasingly complex, with very strong information asymmetries and uncertainties. In this framework, the ability of public authorities to control all the variables in order to effectively protect the general interest is heavily suspected, and a tendency can be perceived for European public authorities to, and market mechanisms seem more adequate for the selection of new technologies and services.

The reform of the telecommunications sector is a very good example of this trend. When telecommunications meant basically telephony, a single and standard service with a clearly defined technology, a public monopoly could take the option to introduce it in the market. When technological progress completely reforms the market, introducing new products and services, with different quality standards and prices, and a high degree of uncertainty, it seems that consumers are better suited for the selection of technologies and services through the free market mechanisms, than a monopolist.

As a result, the creation of laws and institutions specifically devoted to the protection of a particular value of general interest such as the emergence of

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[252] See AMATO, G. and LAUDATI, L. (1999): "When the Economy is Affected with a Public Interest. The protection of Public Interest and Regulation of Economic Activities", in *"The Anticompetitive Impact of Regulation"*, and the examples of workers protection, regional development, or urban development.

competition in monopolised sectors like telecoms, can be framed in a more general and indigenous tendency.

At the same time, the process of the reform of the sector, characterised by the confrontation of different private interest (the monopolist, the business users, the residential users, the equipment manufacturers, the trade unions, etc.), is a good example of how neglecting the relevance of such forces, and the confusion introduced by the consideration of secondary aspects of general interest (influence on inflation or unemployment, for instance) in the decision-making process leads to a lack of transparency and, at the end of the day, democracy.

The regulatory model provides more transparency in the decision-making process, since it is based in the traditional combination of private interests through the political process, and therefore, allows accountability, responsibility and participation. This is particularly important in societies of increasing complexity.

On the other hand, the process of the convergence of the models of public intervention can be recognised in the adoption by the American regulators of very focused but heavily interventionist measures. Schemes such as universal service in telecommunications confirm the derogatory nature of the public intervention. At the same time, formal requirements such as due process and judicial review has been strengthened. Both features confirm the derogatory nature of public intervention as it has been always been perceived in Europe.

4.4. CONCLUSIONS.

81. Final. The elimination of public monopolies not only in the telecommunications sector but in many other economic activities eliminates as

well the more traditional instrument of public intervention in economic activity in Europe.

De-monopolisation and privatisation, nevertheless, do not eliminate the relevance of telecommunications and other network industries for the general well-being and the economic development of modern societies. At the same time, the transition from monopoly to effective competition in network industries faces major challenges which, it is commonly understood, require some kind of public intervention to foster such evolution.

As a consequence, it has been necessary to direct market substitutive intervention using new instruments of public intervention compatible with the competition in the market yet still fully effective.

From this perspective, the rules on competition provided mechanisms to ensure consumer welfare as well as the protection of the competitive character of the markets. However, such rules do not seem fitted to ensure the satisfaction of those general interest objectives which go further than the mere efficiency in the provision of products or services. At the same time, the rules on competition have been designed to protect competition, but not to create it.

As a consequence, other instruments of public intervention were needed. Economic regulation was the answer. Economic regulation can be understood as the continuous and concentrated control of the market by public authorities through the imposition of legal obligations on the private operators, according to their position in the market, in adaptation of the abstract obligations defined by the Legislator, with the objective of ensuring the adaptation of the functioning of the markets to the general interest objectives.

This scheme should not be understood as a mere transplant from the American economic regulation. It is possible to identify tendencies towards this model which are indigenous to Europe. In any case, it is clear that the

American regulatory experience can provide very useful insights about the possibilities, risks and failures of this instrument of public intervention.

CHAPTER 5

COMPETITION LAW v. REGULATION?

SUMMARY: 5.1. Introduction. 5.2. The Limits of Antitrust. 5.3. Regulation Complements Antitrust. 5.4. From Regulation to Competition? 5.5. Conclusions.

5.1. INTRODUCTION.

82. Antitrust v. regulation? Both competition Law and economic regulation have always been, at least in theory, instruments of public intervention for the promotion of the general interest. In the words of an American Judge "regulation and antitrust typically aim at similar goals -i.e., low and economically efficient prices, innovation, and efficient production methods- but they seek to achieve these goals in very different ways".[253]

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[253] *Town of Concord v. Boston Edison Co.* 915 F.2d 17, 22 (1st Cir 1990).

As a matter of fact, it has been shown that both instruments appeared in the US during the same period as part of an attempt to face the challenges created by the development of problematic market structures which had their origin in the industrial revolution. While the rules on competition provided mechanisms for the restoration of the competitive structure of such markets, economic regulation was introduced in order to provide the public authorities with mechanisms for the immediate protection of the general interest, in substitution of the disciplinary role of competition.

In Europe, at that stage, neither the mechanisms of competition Law nor economic regulation were introduced for the correction of those failures in the markets created by the industrial revolution. On the contrary, public authorities monopolised the direct provision of the services and in such a way pursued the satisfaction of the general interest.

The process of liberalisation of the markets, which substantially consists in the substitution of direct public intervention by the discipline imposed by competition in the market as the leading mechanisms of satisfaction of the general interest, has eliminated the traditional instrument of intervention in the European public utilities. European authorities have started to apply to these sectors the rules on competition which had already been introduced for the protection of the competitive structure of the non nationalised markets, and have adopted some of the traditional mechanisms developed in the US for the regulation of the public utilities.

The crucial point is that nowadays, after the general acceptance of the free market mechanisms as being better suited for the satisfaction of the general interest, both instruments of public intervention pursue the satisfaction of the general interest. Competition Law and now also economic regulation have become instruments of the public policy of liberalisation. At the same time, regulation maintains a subsidiary role for the solution of market failures.

Nevertheless, such a role is limited to objectively justified cases and has to be compatible in any event with competition, the leading mechanism of organisation of the telecommunications sector.

83. A complicated but fruitful co-existence. The relationship between competition Law and regulation in the telecommunications sector is complicated for a number of reasons. First is due to the uncertainties that accompany both instruments of public intervention. On the one hand, competition Law does not have a long tradition in some of the Member States and, furthermore, experience on the application of competition Law to industries in process of liberalisation is reduced. On the other hand, regulation is a new instrument of public intervention in most of the European States, particularly in those related to the French administrative tradition. As a result, the role of regulatory authorities and the nature of regulatory mechanisms are not completely clear for all the actors involved in the market.

It is widely believed that sector specific regulation provides a more powerful instrument for public intervention, an instrument that might be necessary to ensure the effectiveness of public intervention. At the same time, it is understood that such kind of intervention might be excessively intrusive and might even obstruct the development of effective competition. A general consensus on the need of regulation exists in Europe. Divergences arise at the point when the extent of such intervention, both in relation to the issues that should be covered by it, and on the temporal duration of the transitory mechanisms, has to be defined[254].

84. The US and the EU experiences. The relation between both kinds of public intervention instruments in the framework of the European reform of the

[254] For an early study on the European framework see HERGUERA, I. and STHEMANN, O. (1997): "Regulation and Competition Policy in the EU Telecommunications Industry", in *Communications & Strategies*, vol. 26, no 2, pp. 141-163.

telecommunications sector cannot be understood without a clear distinction between the European and the American experience.

While in the US there was a long tradition of regulation as an exception to the application of antitrust, in Europe economic regulation has been perceived basically (even if not solely) as an instrument for the liberalisation of the market. As a consequence, economic regulation has not been an exception to competition Law but a complement to it, in such a way, that the fundamental reason for conflict is the similarity and the confusion between both instruments, rather than the disparity in their goals.

85. Evolution in the US. In the US, sector specific regulation has traditionally be considered a potential exception for the application of the antitrust rules. For these were situations in which it was considered that the mechanisms of free competition would not ensure the fulfilment of the general interest. It used to be common wisdom that antitrust was supposed to protect competition and regulation was to restrict price competition and competitive entry, in such a way that both instruments were considered different and even antithetic.[255]

Traditionally, regulation was used as a defence in antitrust suits. On the one hand pervasive regulation could exclude the application of antitrust to a particular activity. On the other hand, sector specific regulation could supersede the antitrust law and create an exemption. Finally, even in those cases in which regulation would not create an antitrust exemption, regulatory obligations in relation to price and entry might have the effect of negating the

[255] See for a very descriptive analyses LOEVINGER, L. (1965): "Regulation and Competition as Alternatives", in *The Antitrust Bulletin*, vol. 10, pp. 101-140; and JOSKOW, P. (1985): "Mixing Regulatory and Antitrust Policies in the Electric Power Industry: The Price Squeeze and retail market Competition", in *Antitrust and Regulation. Essays in Memory of John J. McGowan*, MIT Press, Cambridge, MA, p. 173.

presence of monopoly power.[256] This was the case of the telecommunications sector, where the will of excluding the application of the antitrust rules was one of the leading factors for the emergence of the sectorial regulatory framework.[257]

This view has evolved, as antitrust has been applied to regulated industries and, mostly, as regulation has evolved allowing competition to rule regulated markets.[258] It is only after the deregulation movement that the traditional regulatory mechanisms are considered as tools for the opposite process of elimination of restrictions and the promotion of competition.

The relation between antitrust and regulation in the US is determined not only by the political evolution in respect to the role of public authorities in the economic activity, but also by the position of the rules on competition and on regulatory intervention in the constitutional framework of sources of Law. It is important to note that the Sherman Act has the same normative value as the statues regulating specific sectors, in such a way that the federal Legislator can exclude the application of the antitrust rules to specific activities, whether through express statutory provision, on whether through an implied repeal.[259] In this way, there is no major legal obstacle to the introduction of exceptions to the application of the antitrust rules, as long as such exceptions are clearly established by the federal Legislator.

The relation between the federal antitrust Legislation and the state regulatory actions is necessarily more complicated, due to the fact that issues

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[256] See HJELMFELT, D. (1985): "*Antitrust and Regulated Industries*", John Wiley, New York, p. 268.

[257] *Vide supra* Chapter 2.4. Public Intervention in the US Telecommunications Sector.

[258] See KAUPER, T. (1974): "An Overview", *Antitrust Law Journal*, vol. 43, p. 295; STELZER, M. (1971): "Antitrust and Regulatory Policies: An Introduction and Overview", in *The Antitrust Bulletin*, vol. 16, p. 671.

[259] "When Congress by subsequent legislation establishes a regulatory regime over an area of commercial activity, the antitrust laws will not be displaced unless it appears that the antitrust and

related to federalism arise. According to the state action doctrine, founded on in *Parker v. Brown*,[260] states can exclude the application of federal antitrust law as long as the state does not unduly burden interstate commerce,[261] what is ensured in those cases where the state acts in the traditional government functions and when state actions do not irreconcilably conflict with the *per se* violations of the Sherman Act. The state action doctrine has evolved as so to include exclusively acts that reflect the sovereign position of the state, understood as Legislator actions, excluding decisions adopted by subordinate state actors such as municipalities or the regulatory agencies.[262]

86. Situation in Europe. The European situation is widely different. On the one hand, after the de-monopolisation and the privatisation of the telecommunications sector, the regulatory framework has been introduced in order to favour the development of competition. Regulatory obligations in Europe are definitely connected to the promotion of competition in liberalised markets rather than to the exemption to the application of the rules on competition as was the traditional case in the US.[263]

On the other hand, the relationship between competition Law and sector specific regulation is decisively influenced by the supremacy of the rules on competition defined in the EC Treaty. Under the *effet outil* doctrine, defined by the ECJ, Member States cannot "enact measures enabling private undertakings to escape from the constraints imposed by Articles 85 to 94 of the Treaty [now 81 to 90]".[264] As a result, "under Community Law national authorities,

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regulatory provisions are plainly repugnant", *City of Lafayette v. Lousiana Power & Light*, 435 U.S. 389, 398 (1978).

[260] *Parker v. Brown*, 317 U.S. 341 (1943).

[261] AREEDA, P. (1981): "Antitrust Immunity for 'State Action' After Lafayette", in *Harvard Law Review*, p. 435.

[262] SHENEFIELD, J. (1982): "The *Parker v. Brown* State Action Doctrine and the New Federalism of Antitrust", in *Antitrust Law Journal*, vol. 51, p. 337-347.

[264] Case 13/1977, *GB-Inno-BM/ATAB*, 1977 ECR 2115, paragraph 34.

including regulatory authorities and competition authorities, have a duty not to approve any practice or agreement contrary to Community competition law". "If a NRA were to require terms which were contrary to the competition rules [...] the Member States itself would be in breach of Article 3(g) and Article 5 of the Treaty, and therefore subject to challenge by the Commission under Article 169".[265] The application of the exception defined in Article 86(2) EC Treaty was excluded by the Commission Directives upheld by the ECJ, and only a modification in the market conditions would allow the application of the exception in the telecommunications markets.

As a result, the relevant differences between the American and the European environments prevent a simple transplantation of the institutions and instruments of indirect public intervention and the balance that exists between them.

5.2. THE LIMITS OF ANTITRUST.

5.2.1. Introduction.

87. De-monopolisation was not enough. The process of the liberalisation of European telecommunications markets entails the substitution of public leadership in the development of the sector by a demand-driven leadership through the traditional mechanisms of competition in the market.

It is evident that the first step in the process of the liberalisation of European telecoms was the elimination of the special and exclusive rights. It has been studied how the Commission pursued such goal through a step-by-

[265] See Notice on the application of the competition rules to access agreements in the telecommunications sector. Framework, relevant markets and principles, OJ 1998 C 265/2, paragraphs 13 and 61. The application of an Article 169 procedure in such cases has been upheld by the Court in Case C-35/96, *Commission v. Italy*, 1998.

step strategy. It is equally clear that the mere elimination of special and exclusive rights was only the first measure in the liberalisation of the markets. That process would only be completed upon the emergence of effective pressures on all the market players to satisfy consumers' demand.

It is obvious that the entrance to the market of new comers, and the emergence of effective competition among these new comers and the incumbents, could not be directly guaranteed by public authorities. Nevertheless, those authorities did have some options. Firstly, they could avoid any intervention, expecting private entities to enter the market and succeed in challenging the monopolistic position of the incumbent. Secondly, they could foster the emergence of competition by levelling the playing field in favour of the new comers.[266]

It was always clear that a structural intervention in favour of the new comers such as the break-up of the incumbents was excluded. Nevertheless, it was commonly agreed that some kind of public intervention would be necessary in order to accelerate the transition from a public monopoly to a competition-driven market. Otherwise, public monopolies could be substituted by private monopolies with no effective pressure to satisfy consumers' demands.

There was no doubt that the major obstacle to competition was the presence of the incumbents. Since no structural measure was undertaken, the former legal monopolists enjoyed the control of the only universal telecommunications network in each Member State, a facility which would it take years to duplicate despite the availability of new technologies. Furthermore, the incumbents benefited from a 100% market share in all the formerly monopolised service markets (from fixed telephony to value-added

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[266] See Teligen Ltd (2000): "*Study on Market Entry Issues in EU Telecommunications Markets after 1st January 1998*", European Commission, Brussels.

services). As a consequence, they benefited from the relevant economies of scale and scope, as well as from the well-known network externality effect. The brand-recognition, financial capability and political power of the incumbents strengthened the position of the former monopolists the very day their exclusive rights were lifted.

The disconnection between costs and prices of the incumbent, which allowed new comers to dispose of attractive margins in some market segments. At the same time, new comers, unlike the incumbent, did not face the burden of inherited, out-dated technologies or inefficient structures. All of this allowed new comers to enter the market and establish themselves, but never to put effective pressure on the incumbents in the more important market segments: infrastructures and the fixed telephony service.

The incumbents controlled the public fixed telephony network, the only universal telecommunications network available at that moment. Such control was particularly relevant as regards the access network, the so-called "last kilometre", due to the technical and economic difficulties to duplicate such an infrastructure in a short period of time. The control of the public fixed telephony network by the incumbent was perceived as the main barrier to entry, and as a consequence, the efforts of the public authorities were focused on the development of mechanisms that would eliminate such barrier.

5.2.2. Antitrust and Market Power.

88. Market dominance. The point of departure of European antitrust with regard to market power is the notion of market dominance. Market dominance is defined by the ECJ as the "position of economic strength enjoyed by an undertaking which enables it to hinder the maintenance of effective competition on the relevant market by allowing it to behave to an appreciable

extent independently of its competitors and customers and ultimately of consumers".[267]

The telecommunications incumbents enjoyed dominant positions for decades thanks to the exclusive rights granted by the relevant public authorities.[268] As it has been put by the Commission "the mere ending of legal monopolies does not put an end to dominance. Indeed, [...] the development of effective competition from alternative network providers with adequate capacity and geographic reach will take time".[269] Furthermore, the significant dominance of the former monopolies in the infrastructure markets might be extended to a number of vertically related markets, as it puts them "in a situation comparable to that of holding a dominant position on the markets in question as a whole".[270]

It is interesting to note that Community competition Law distinguishes different regimes for undertakings with market power according to its origin.

89. Article 82. On the one hand, dominance can have its origin in the efficiency of the undertaking and its growth in the market through competition. In such cases, the regime established in Article 82 EC Treaty (former 86) is applied. According to this provision, as it has been interpreted by the ECJ, this kind of market dominance is not prohibited, nor even recriminated. In the words of the ECJ "a finding that an undertaking has a dominant position is not in itself a recrimination but simply means that [...] the undertaking concerned

[267] Case 322/81, *Michelin v. Commission*, [1983] ECR 2461.

[268] An undertaking with a exclusive right in a substantial part of the common market can be considered to enjoy a dominant position, Case 311/84, *CBEM/CLT*, [1985] ECR 3261.

[269] *Vide* Access Notice, paragraph 64 (*supra* footnote 265).

[270] Case C-333/94 P, *Tetra Pack International v. Commission*, [1996] ECR I-5951.

has a special responsibility not to allow its conduct to impair genuine undistorted competition on the common market".[271]

Thus, the Treaty (as well as the national legislations) does not provide mechanisms to modify the market structure, that is, the dominance itself. On the contrary, it merely provides mechanisms to obstruct certain behaviours of the dominant undertakings. Competition authorities only intervene against behaviours contrary to Article 82 *ex post*, in order to ascertain the anticompetitive character of such behaviour and to impose the correspondent sanction.

90. Merger Regulation. Before the adoption of the Merger Regulation in 1990, concentrations with anticompetitive effects could only be blocked under Article 82 EC Treaty when they supposed the strengthening of a dominant position, but not when dominance was the result of the concentration.[272] The adoption of the Merger Regulation modified the approach to market power when it was the result of a merger or acquisition.

In this case, the Community policy is now to control the market structure and to obstruct the concentrations that would "create or strengthen a dominant position as a result of which effective competition would be significantly impeded in the common market or a substantial part of it".[273] If dominant positions due to efficiency in the market are respected by Article 82 EC Treaty, dominant positions due to operations foreign to the regular functioning of the market are blocked by the competition authorities.

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[271] Case 322/81, *Michelin v. Commission*, [1983] ECR 3461.

[272] "The strengthening of the dominant position of an undertaking may be an abuse and prohibited under Article 86 of the Treaty, regardless of the means and procedure by which it is achieved", Case 6/72, *Europemballage and Continental Can v. Commission*, [1973] ECR 215, paragraph 27.

[273] Article 2(3) of the Merger Regulation.

The rules on concentrations allow the European Commission to adopt an *ex ante* decision based on the effects of the concentration upon market structure.

91. Article 86. Finally, market dominance can be the result of the exclusive or special right granted by a public authority for the provision of a service of general economic activity. The special or exclusive rights are scrutinised by the Commission with the powers granted by Article 86 (former Article 90), and only accepted if the restriction to competition is necessary for the fulfilment of the general economic interest.

The point is that, when the exclusive rights are considered incompatible with the Treaty and therefore eliminated, the linked dominance cannot be eliminated by the competition authorities, despite its 'illegitimate' origins. The somehow 'illegitimate' dominance enjoyed by the former monopolists can be compared with the dominance reached through mergers and acquisitions, in the sense that both are linked not to the growth in the market, but to actions foreign to the competitive process. The difference in the legal regime of both dominance is that a particular mechanism to control market structure was adopted in the case of concentrations, while in the case of de-monopolisations no particular mechanism exist, in such a way that no structural intervention can be adopted with the mechanisms provided by the rules on competition.

As a result, market dominance originated by exclusive rights granted by public authorities, even if declared contrary to the Treaty, is subject to the general regime defined by Article 82 EC Treaty for the firms that reached such position through growth in the market. The former monopolies enjoy the positive attitude towards efficiency and the respect for the dominance reached thanks to it, which defines the Article, 82 regime. The result is that their dominance is respected, and competition Law only provides *ex post* mechanisms for the control of their abusive behaviour.

5.2.3. Antitrust and the Promotion of Competition.

92. Exclusionary behaviour by the incumbents. The already long tradition of application of the rules on competition has identified a number of categories of behaviours with anticompetitive effects. Predatory pricing, refusals to deal, and other exclusionary practices can be implemented by the incumbents in order to hinder the growth of competition in the telecommunications markets. Competition authorities have mechanisms to obstruct such practices and even to impose penalties to the undertakings which implement them. As a matter of fact, both Community and national competition authorities have already intervened in order to eliminate exclusionary behaviours by dominant undertakings in the telecommunications markets and in some cases very significant fines have been imposed.

Nevertheless, the application of the competition rules on exclusionary practices might not always be as efficient as required by the exceptional situation created by the de-monopolisation of the telecommunications markets. The cumbersome procedures under both the national and the Community competition authorities might not effectively reduce the potential barriers introduced by the incumbents, as the *ex post* application of such rules might arrive too late, once the new comer has been excluded from the market.

93. Structural obstacles to competition. The European rules on competition proscribe behaviours of the incumbents directed to obstruct the emergence of competition in the liberalised market (exclusionary practices). Nevertheless, such rules do not provide mechanisms to modify the market structure inherited from decades of the monopolisation of the market by public authorities. The rules on competition do not provide mechanisms which actively promote entry to the market by new comers by the elimination of those barriers to entry which are not connected to the incumbents behaviour.

The existence of two important obstacles to competition in the telecommunications industry as well as in most network industries has been widely recognised. A first structural obstacle is the network externality effect. A network increases its value as it increases the units connected to the network. A network which only connects one unit has a value of zero. A network that connects all the existing points has the maximum potential value. As a consequence, a small network without universal coverage developed by a new comer will rarely be able to compete with the universal network of the former monopolies. This leads to a winner-takes-it all result in network industries.

The second structural obstacle is the existence of important economies of scale. Traditionally, it was considered that such economies reached the totality of the investment, in such a way that the sector had an unavoidable tendency towards monopolisation by one undertaking. The telecommunications market was considered a natural monopoly. Technological development and the apparition of new infrastructures (satellite, fibre etc.) and services (i.e. IP telephony) has changed dramatically the structure of the sector which is not considered anymore a natural monopoly. In any case, it is evident that economies of scale are still present in the telecommunications markets. Economies of scale might not be relevant with regard to most telecommunications services markets. In relation to networks, it seems that for most market segments economies of scale do not reach the whole investment as they become exhausted at an early stage. As a consequence, there is some scope for competition, even if in many cases restricted to a limited number of companies.

These structural obstacles are reinforced by the dominant presence of the former monopolies. As no structural measure was adopted by the public authorities, the former monopolies enjoyed a 100% market share in most telecommunications markets right after de-monopolisation. As a matter of fact,

such market share has not decreased significantly in important markets such as the local loop or the local telephony service.

As a consequence, the most important obstacle to competition in the telecommunications sector after de-monopolisation would be not the behaviour of the former monopolies itself, but the market power they would have enjoyed as a consequence of being the sole beneficiary of the network externality effect and the economies of scale derived from their universal network.

Even if competition Law provides the mechanisms for the obstruction of the behaviours which might reinforce or extend the dominant position of the incumbents, competition Law does not provide specific mechanisms to treat market dominance based on an exclusive right that has been eliminated because of its incompatibility with the Treaty. Even if the apparition of a competitive environment is a fundamental element of the process of reform of the telecommunications markets, competition Law lacks mechanisms to reduce the barriers to entry derived from the network externality effect and the economies of scale.

Former monopolists receive the treatment designed for the undertakings that acquired a dominant position as the result of growth through competition thanks to their efficiency, a treatment based on the respect of the dominant position and devoted merely to the obstruction of the abuses of such dominance.

Competition authorities might be tempted to expand the application of the rules on abusive behaviour so as to cover the cases under evaluation. It might even be the case that certain cases are on the border line of the case-law with regard to the abuse of a dominant position, as it is not always simple to distinguish between the effects of the behaviour of the undertaking and the effects of the mere structure of the market.

Such temptations, even if they might result in the solution of sector specific problems, entail important risks of de-naturalisation of the rules on competition and the extension of the precedent to other areas where they might have dangerous results. It is for this reason that the competition rules on abusive behaviour should not be applied for the reduction of barriers to entry derived from the mere market power of the former monopolists.[274]

5.2.4. Antitrust and Exploitative Practices.

94. Exploitative abuses. As special and exclusive rights were eliminated, the problem was not only to foster the emergence of competition, but also to ensure that in the transitory period, the incumbents would not try to obtain monopoly rents from consumers.

Initially, European antitrust was only concerned with practices directed at obtaining monopoly rents from consumers. It was sustained that Community competition Law had opted for a differentiation in respect to American antitrust law, not through the persecution of the attempts to monopolise, but through the abuses of the monopolistic position, without considering the origins of such dominance.

American antitrust lawyers always criticised the notion of exploitative abuses. It has been stated that it "has not an entirely antitrust connotation".[275] They were right, as the notion of exploitative abuses does not protect the competitive process which is considered to foster consumer welfare, but tries to ensure consumer welfare through the control of the behaviour of the dominant company. This is something that is closer to the American regulatory tradition.

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[274] *Vide infra* Chapter 10. Conclusions: From Regulation to Competition?

[275] RAHL, Statement in International Aspects Of Antitrust, Hearings Before the Subcommittee on Antitrust and Monopoly of the Senate Committee on the Judiciary, 89th Cong. 2d Sess, Part. 1, 385 (1966), in JOLIET, R. (1970): "*Monopolization and Abuse of Dominant Position. A Comparative Study of the American and European Approaches to the Control of Economic Power*", Martinus Nijhoff, Den Hague, p. 247.

As a consequence, it can be said that the European rules on competition had a strong regulatory flavour, as their focus was not on proscribing the monopolisation of the market (as in the US) but in prescribing behaviours in markets with distortions originated by the market power of dominant firms. In Europe the lack of regulatory tradition, rules and institutions may have forced antitrust authorities to adopt a regulatory approach that could not be implemented by non-existent regulatory institutions.

Such an approach, however, has always introduced difficulties for the application of the notion of exploitative abuses. Antitrust authorities do not have the resources to follow closely the evolution of every singe market in order to individuate whether a particular price or condition is fair for the consumer. It is not very clear either what are the criteria to be used in order to evaluate the fairness of contracting conditions. Furthermore, the rules on competition only allow for the proscription of contracting conditions, but never for the prescription of them that would be necessary in order to immediately ensure consumer welfare.[276]

It was only after the intervention of the ECJ in the 70's through judgements such in the *Continental Can* and *Hoffman-La Roche* cases that the anti-competitive role of such provision was confirmed.[277] Exclusionary practices devoted to obstruct or exclude the development of competition in the dominated market were also considered contrary to Article 82 EC Treaty.

As a matter of fact, due to the influence of the Chicago School and the introduction of economic reasoning in the antitrust decisions, the tendency in

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[276] "The Commission stated in 1975 that measures to halt the abuse of dominant positions cannot be converted into systematic monitoring of prices. In proceedings against abuse consisting of charging excessively high prices, it is difficult to tell whether in any given case an abusive price has been set for there is no objective way of establishing exactly what price covers costs plus a reasonable profit margin", Fifth Report on Competition policy (1975), point 3.

[277] TEMPLE LANG, J. (1979): "Monopolisation and the Definition of 'Abuse' of a Dominant Position under Article 86 EEC Treaty", in *Common Market Law Review*, vol. 16, pp. 245-364.

the last decades has been to focus the intervention of the antitrust authorities in the obstruction of exclusionary practices and to reduce intervention against exploitative practices, even if the wording of Article 82 makes direct references to exploitative practices which have to be prosecuted by the European antitrust authorities.

The risk of the obtention of monopoly rents was particularly high in the telecommunications markets after de-monopolisation as telecommunications former monopolists enjoyed a pervasive market power in important market segments. They could impose abusive contractual conditions on providers and clients, in relation to quality, or impose low prices on providers and excessive prices on clients. The very same risk existed before the de-monopolisation, but it was considered that the public nature of the monopolist would ensure fairness in the contractual relations with the monopolist.[278]

In any case, and despite the evolution of European antitrust, the EC Treaty as well as many national legislations still provide legal mechanisms to proscribe abusive behaviours.[279] Community authorities have made clear that even if the implementation of the exploitative abuses notion, in particular against excessive prices, is extremely complicated in the telecommunications market due to the difficulty in defining cots,[280] they will not hesitate to apply Article 82 when necessary.[281]

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[278] Nevertheless, the fairness was only ensured politically, in such a way that providers and clients of the monopolist did not dispose of juridic instruments to enforce such fairness.

[279] Even if the proof of the abusive character of a condition, for instance a price, is not simple, there are precedents in Community Competition Law of prices considered excessive and, therefore, null. See for instance ECJ C-226/84, British Leyland v. Commission, ECR [1986] 3263.

[280] *Vide infra* Chapter 9.2.3. Compulsory Access.

[281] As has been stated by two relevant Commission officials, "The Commission itself never aspired to use Article 86 EC Treaty in order to act as a price setting authority. [...] however, it has also become clear that the Commission will make full use of its powers under Article 86", HAAG, M. and KLOTZ, R. (1998): "Commission Practice Concerning Excessive Pricing in Telecommunications", in *Competition Policy Newsletter*, vol. 4, no. 2, pp. 35-38.

5.2.5. Conclusion: The Regulatory Tendency of European Antitrust.

95. Conclusion. The market power of the telecommunications incumbents was so pervasive after de-monopolisation that it was commonly understood that the rules on competition were not enough to ensure consumer welfare. Even the Commission recognised that "Community Competition rules are not sufficient to remedy all of the various problems in the telecommunications sector".[282]

As it has been described, the rules on competition basically proscribe behaviours that might reduce the pressures of effective competition and therefore damage consumers. As regards undertakings with significant market power, the rules on competition prohibit behaviours directed to maintain or expand the market power of the dominant firm. Such rules cannot ensure that a company without the pressure of competition respects consumers welfare, and certainly, they are not designed to put an end to the dominant position. The main reason is that an active intervention through prescriptive obligations would be necessary to ensure such objectives, and antitrust does not provide such a possibility.

96. The regulatory tendency. The European rules on competition, particularly those against abuse of dominant position, present a strong regulatory tendency. Article 82 EC Treaty, as originally interpreted after the adoption of the Treaty, entails an approach to market power which somehow abandons the American approach to antitrust in order to get closer to the regulatory intervention which had developed in the US by the end of last century.

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[282] *Vide* Access Notice, paragraph 14 (*supra* footnote 265).

Article 82 EC Treaty and its national counterparts do not outlaw dominant positions. These provisions obstruct the abuse of such dominance through the prohibition of certain behaviours that would objectively entail such an abuse.

Originally, the attention of the competition authorities was solely focused on those abuses with exploitative effects. In this way, effects such as excessive pricing, the imposition of unfair trading conditions or discriminations were forbidden. Fairness in the trading activities of the dominant undertakings was the key of the public intervention. Little attention was paid to the competitive process or even to the competitive structure of the market.

In this way, the rules on competition allowed public authorities not to control the competitive character of the market, but to ensure the fairness of the behaviour of the strongest companies, that is, to regulate market power.

The evolution of European competition Law introduced firstly the proscription of exclusionary practices. Secondly, the attention was shifted from fairness to efficiency and consumer welfare. In this way, the European rules on competition evolved towards a more orthodox approach directed to protect competition as a dynamic process and the beneficial effects for consumers of effective competition. The European rules on competition, particularly after the influence of the Chicago School, had abandoned the regulatory approach and strengthened the features that characterised traditionally American antitrust.

Nevertheless, the permanence in the Treaty of provisions which allow a quasi regulatory intervention by competition authorities, and the will of these authorities to apply the rules on competition in liberalised markets in order to solve the specific conflicts derived from the reform of such markets entail the risk of a return to the regulatory origins of European antitrust.

Furthermore, and despite the intrinsic limitations of the rules on competition, the Commission has tried to make use of such a set of rules firstly to foster the de-monopolisation of the sector, and secondly, to modify the

structure of the market by reducing the structural obstacles faced by new comers to the telecommunications markets.

5.3. REGULATION COMPLEMENTS ANTITRUST.

5.3.1. Regulation for the Promotion of Competition.

97. The role of regulation. It was a common assumption in Europe that the rules on competition were not sufficient to ensure the emergence of effective competition in the European liberalised telecommunications markets, and that new instruments of intervention had to be established in order to provide mechanisms for the implementation of the policy to actively promote the emergence of such competition.

Economic regulation, the traditional instrument of indirect intervention in the US, provided an interesting model, and many of the mechanisms which had been developed in that country were transplanted in order to conform an instrument for indirect intervention in liberalised markets. The mechanisms of concentrated control of the market and imposition of specific legal obligations on the private actors in order to satisfy the general interest were particularly well-suited for the telecommunications markets, as they allowed for the imposition of different obligations upon the undertakings depending on their position in the market.

While the rules on competition proscribe exclusionary behaviours by the incumbents, regulatory obligations can not only proscribe certain behaviours, but also prescribe measures which on the one hand ensure that no exclusion will take place, whilst on the other, go further in reducing the obstacles derived from the market structure.

It is important to underline that in Europe, regulation has as its main goal the promotion of competition. The situation, therefore, is quite different from the American experience, where regulation has usually been perceived as an obstacle to competition and only recently regulation has become another instrument for the promotion of competition in the traditionally regulated markets.

98. Regulation follows antitrust. European public authorities had a wide choice of regulatory strategies for the liberalised telecommunications markets. It is interesting to note that the regulatory framework finally adopted respects the same basic principle in which the competition rules on abuse of dominant position are based: the special responsibility of the operator which enjoys market power. Furthermore, many of the regulatory instruments (the notion of operators with significant market power, SMP, for instance) and obligations (pricing policy, network access etc.) follow closely the existing antitrust model.

It could be said that sector specific regulation for the promotion of competition departs from the rules on competition, extends its principles, and completes it, providing more effective mechanisms for the obtention of similar goals.[283] Nevertheless, it should be always understood that there are important differences in scope and mechanisms of intervention between both instruments of public intervention. The regulatory framework designed by the European authorities goes a step further than the rules on competition. It introduces obligations directed to reduce the incumbent's market power through mechanisms which force them to share with the new comers some of the

[283] The heavy influence of Competition Law on telecommunications regulation has been pointed out in FORRESTER, I. (2000): " Achieving and safeguarding conditions for fair and efficient competition" in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gossling Ed., Hart, pp. 585-614.

benefits derived from such power, based on the assumption that somehow, such power has an 'illegitimate origin'.

99. Significant market power. Just as the notion of dominance delimits the application of the Article 82 EC Treaty, the regulatory category of operators with significant market power has been introduced in the Community Directives in order to delimit the ambit of the application of regulatory obligations. Article 4(3) of Directive 97/33/EC establishes that an operator "shall be presumed to have significant market power when it has a share of more than 25% of a particular telecommunications market".[284]

Important differences exist between both notions. The most obvious one is that the notion of operator with significant market power is far less exigent than the notion of dominance. As a matter of fact a market share of 25% would only in extreme cases be qualified as dominance under Article 82 EC Treaty.[285] It is not simple to justify such a reduction of the requirement, as the asymmetry is supposed to be introduced in order to reduce the burden for the new comers of the barriers to entry derived from the presence of the former monopolies. The application of the regulatory obligations defined for the operators with significant market power to a new comer which reaches such a position thanks to the efficient provision of its services seems contrary to the very same principles of the regulatory framework. A possible explanation for such

[284] Article 4(3) of Directive 97/33/EC allows NRAs to include in the category operators with a lower market share, as well as to exclude operators that exceed it, according to objective criteria defined in this provision and in paragraph 6 of the preamble, criteria that, on the one hand resemble in a large extend the criteria for the attribution of market dominance (turnover relative to the size of the market, access to financial resources, experience etc.), and on the other, include particularities of the telecommunications markets (as in the case of the control of the means to access end-users).

[285] It is commonly shares that a market share under 30% would not imply a dominant position if not accompanied with very exceptional market circumstances, BELLAMY & CHILD (1993): "*Common Market Law of Competition*", Sweet & Maxwell, London, p. 604. Nevertheless, in the words of the Commission "a dominant position cannot even be ruled out in respect of market shares between 20% and 40%", X Report on Competition Policy, 1980, point 150.

inclusion is the intention to provide regulatory mechanisms of intervention similar to the antitrust figure of collective dominance.

There is a procedural difference between both notions. While dominance is determined *ex post* for a specific conflict, SMP is determined *ex ante* in order to subject an operator to a series of regulatory obligations. As a result, the definition of the relevant markets has to be done in abstract, without reference to a specific conflict or behaviour. The abstract nature of the definition of the market requires defining wide markets in order to cover all the possibilities towards the future. On the contrary, the definition of the relevant market in Competition Law is done *ex post* for a specific case, in such a way that the definition of the relevant market can be adapted to the specific conditions of the case and a very reduced market can be defined.

These two formal differences allow identifying the more important difference between both notions. Market dominance is a more objective criterion. The competition authorities merely certify that a particular undertaking enjoys a significant degree of market power in a particular product and geographic market which allows it to behave independently from competitors and consumers (that is, without the constraints of competition), which in turn allows it to develop certain practices which could damage the very same competitive process and, therefore, consumers. Significant market power, on the contrary, is a subjective classification according to certain agreed criteria. It is not such market power that really creates an obstacle to competition. On the contrary, market power is merely used as a criterion to impose regulatory obligations. Such obligations are not directly derived from the risks originated by market power, but from the market structure in which such power is held. This is the weakness of the notion of operator with significant market power, as will be demonstrated in the following pages.

100. Regulatory intervention. Most of the regulatory mechanisms are closely linked to the antitrust mechanisms of intervention. The leading example is the regulation on network access. It is not difficult to see the evolution from the antitrust essential facilities doctrine to the Open Network Provision framework.[286] Similar examples can be identified with regard to pricing policy (not only between competitors but also for final consumers) and in particular with regard to minimum and maximum prices.

It is possible to identify how the regulatory framework departs from the rules on competition and extends its reach in two lines. On the one hand, the regulatory framework provides more effective mechanisms of intervention in order to obstruct practices that could damage competition as well as final consumers. The *ex post* antitrust intervention is complemented with an *ex ante* regulatory intervention with the same goals and very similar objectives and even content. On the other hand, the regulatory framework goes a step further and introduces obligations that would not usually be included under the antitrust regime, or in any case would be on the borderline of the antitrust rules.

This further step is usually related to the specific market structure of the sector and the will of public authorities to allow new comers to overcome the difficulties created by economies of scale and the network externality effect. This is particularly the case of the regulatory framework on network access.

5.3.2. Regulation for the Immediate Protection of the General Interest.

101. Regulation and the exploitative abuses. Regulatory mechanisms have an important role to play in order to ensure the satisfaction of the general interest in the liberalised telecommunications markets. Regulatory intervention might be necessary to impose on the operators obligations for the immediate

[286] *Vide infra* Chapter 9. Sector Specific Regulation on Network Access.

protection of the general interest. Such obligations seem necessary during the transitory period to effective competition, since the risk of exploitative abuses by the incumbents is particularly high.

During the transition period from monopoly to effective competition, the former monopolies enjoy such a strong dominance in particular markets, that they can be tempted to obtain monopoly rents, rents which might be useful to obstruct the development of competition in more dynamic market segments. Competition Law provides mechanisms to avoid such exploitative abuses of dominant position, but these mechanisms are not fully effective,[287] particularly in a situation where there is a tendency for these abuses to be more common, as is the case of recently liberalised telecommunications markets.

The fact that competition rules can only be applied *ex post* reduces their efficacity, particularly if the effective application of such solutions requires a long period of time. Competition authorities cannot spend their limited resources in a comprehensive control of the price and quality conditions of the services provided by the former monopolies, and neither can spend their resources in endless procedures each time a consumer considers that prices charged by the operator are excessive.

Most of the national regulatory authorities have at their disposition mechanisms of intervention aimed at avoiding exploitative abuses in the transition period to effective competition. Firstly, NRAs use mechanisms to impose on the former monopolists the obligation to communicate the relevant information in relation to tariffs and quality of their services according to objective standards. The transmission of this information to the consumers, at the same time as the creation of standard contracts, with the obligatory inclusion of clauses related to quality standards and pricing devoted to the

[287] *Vide supra* Chapter 8.4. The Limitations of the Essential Facilities Doctrine.

introduction of transparency in the provision of the services by the former monopolies might be sufficient for the protection of the final users.

In case such preventive mechanisms are not enough, NRAs can impose the maximum prices, or even fixed prices, as well as specific obligations in relation to the quality standards of the services provided by those operators with a significant market power.

102. A new model of protection of the general interest. A very important result of the process of reform is the imposition by the Community authorities of legal obligations on the Member States to guarantee the satisfaction of certain general interest objectives. The particular structure of the European Union has facilitated, for the first time, the transformation of the traditional political responsibility on the provision of services of general interest, by a legal responsibility, as Community directives on telecommunications define specific obligations for the Member States.[288]

Member States have, thus, the legal obligation to ensure the fulfilment of certain objective of general interest. At the same time, Member States can define other objectives of general interest not included in the Community Directives. One of the leading principles of the new model of public intervention for the protection of competition is subsidiarity. The reform of the sector is based on the confidence in the market for the ruling of the telecommunications markets. Since public intervention can obstruct the regular functioning of the market mechanisms, it has to be restricted, in the sense that public authorities should only intervene in case competition in the market cannot ensure the satisfaction of the general interest.[289]

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[288] Just as an example, see Article 3 of Directive 98/10/EC "Member States shall ensure that the services set out in this Chapter are made available to all users in their territory, independent of geographical location, and, in light of specific national conditions, at an affordable price".

The regulatory model imposed by the Community authorities for the Member States' intervention for the immediate protection of the general interest is based on the indirect intervention of the public authorities. The national public authorities define and impose on the private operators in the market the necessary obligations in order to ensure the satisfaction of the general interest. Two are the main consequences of this policy. On the one hand, clarity is introduced in the system, as the general interest is not anymore a vague and diffuse principle which legitimise any public action. Given that specific obligations have to be imposed on the operators, the new model requires the definition of the general interest and its implications.[290] On the other hand, the obligations imposed on the providers of the service create parallel rights on the consumers, who finally can identify the services and conditions of the provision of such services which are considered of general interest, and, furthermore, dispose of mechanisms for the enforcement of such obligations.

103. New mechanisms of protection of the general interest. The asymmetric regulation model provides mechanisms of public intervention for the immediate protection of the general interest. Such mechanisms have to be compatible with the competitive structure of the market, and at the same time effective. Such mechanisms are always based on the imposition of specific obligations on the operators in the market, with a particular preference for the operators with significant market power.

Public authorities can impose on the operators obligations to provide services which they would not provide under regular circumstances due to the lack of economic incentives. On the same way, obligations in relation to the

[290] In those cases in which public services were not directly provided by the public authorities but by private operators under concession rights, the specification of legal obligations imposed on the concessionaire was also common. Nevertheless, the particular relation between the public authority and

conditions of the provision can be imposed, for instance on relation to quality (minimum quality) or price (maximum price or even a fixed price). In this way, public authorities can ensure, for instance, that every citizen has access to those services considered indispensable, at an affordable price and with the appropriate quality standards.

The asymmetry in the imposition of obligations in relation to the immediate satisfaction of the general interest can promote the development of competition on the market. At the same time such a asymmetry can ensure the effectivity of the general interest defence, as the operators with a stronger position (comprehensive presence in all the territory, more experience etc.) are in a better position to ensure the fulfilment of the general interest objectives.

5.3.3. The Risk of Over-Regulation.

104. Weakness of the regulatory structure. The main weakness of the European regulatory framework is that it is based on the classification of an operator under the category of SMP according to its market share when this is not the reason for the imposition of regulatory obligations. The regulatory framework is really imposed due to the existence of market failures deriving from the long lasting exclusive rights, from the tendency of the market to monopolisation, or from both reasons at a time. The problem is that market share and therefore SMP does not reflect the existence of market distortions, but merely the existence of at least one operator with an important market share.

As a result, the same regulatory framework is imposed independently of the reason why the holding has a market share of more than 25%. Such a market share can be the result of fierce competition that has eroded most of the

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the concessionaire (often a monopolist) did not traditionally introduce a lot of transparency in the relationship.

market share of the incumbent, but equally includes a higher market share of an efficient operator, or an incumbent that maintains an almost absolute control of a market due to the structural obstacles to competition originated by economies of scale or the lack of demand.

Such a scheme has not created major concerns in the period following the de-monopolisation. Market distortions were present in almost every segment of the telecommunications markets as a consequence of the long lasting exclusive rights of the incumbents. The potential distortions of the regulatory policy were overcome by the beneficial effects of the emergence of competition.

Nevertheless, as the markets have evolved, and effective competition emerges in some market segments but not in others, or at least not at the same speed, the regulatory scheme, and in particular the SMP category in which it is based, might start to distort the telecommunications markets. Once new comers have accessed the different telecommunications markets, it is important to review the effects of such a scheme.

It is possible to identify markets where important market failures exist independently of the presence of the former monopolist. It is clear that in some markets there is limited scope for competition or even no room at all. This seems to be the case of some access markets, particularly in rural areas.

105. The risk of over-regulation. The leading principle established by the Community authorities in relation to regulation is subsidiarity, in the sense that public intervention has to be restricted to those occasions in which it is necessary. As a result, regular market mechanisms are trusted also for the development of the effective competition in the telecommunications markets, and regulatory intervention is devoted, primarily, to complement such mechanisms, by the introduction of elements directed to impose on operators with significant market power, the pressure that competition would impose on them. When these mechanisms are not sufficient, more aggressive mechanisms

are introduced, aimed at substituting the market by the imposition of the results that would be reached by competition in the market.

It is important to note that this kind of intervention has a transitional character. Once competition has emerged, this intervention should disappear. The obligations imposed for the reduction of barriers to entry once competition has emerged in the telecommunications markets is established by Community Directive 97/33/EC,[291] and Directive 97/51/EC.[292]

Intervention by public authorities in economic activity, and in general in the exercise of public power, reveal tendencies that go against the transitional character of the regulation for the promotion of competition and might complicate its elimination in the future. The result could be the future over-regulation of competitive markets and the distortion of competition by the maintenance of asymmetric regulation. The tendency of public intervention mechanisms to expand to include more elements of the activity subject to public intervention and to neighbouring activities has been studied. Secondly, the phenomenon of regulatory capture might complicate the elimination of regulation given that those groups benefited by the asymmetry will certainly lobby for the maintenance of such rules.

It is for this reason that some Member States have introduced specific provision in their telecommunications legislation in order to facilitate the elimination of transitional regulatory obligations. Such is the case of Germany

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[291] "When effective competition is achieved in the market, the Competition rules of the Treaty will in principle be sufficient to monitor fair competition *ex-post* so that the need for this Directive will be reconsidered, with the exception of the provisions on universal service and the settlement of disputes", paragraph 25 Directive 97/33/EC.

[292] "Until an effective competitive environment is achieved, there is a need for the regulatory supervision of tariffs for leased lines with a view to ensuring cost orientation and transparency in accordance with the principle of proportionality, where it is appropriate to allow the requirements for cost orientation and transparency in specific markets to be set aside where no organisation has significant market power or where effective competition ensures that tariffs for leased lines are reasonable", paragraph 15 Directive 97/51/EC.

or the Netherlands, where a so called "sunset clause" has been introduced according to which the evolution of the telecommunications markets will be regularly scrutinised after a certain date, so that when a satisfactory degree of competition has emerged, the decision to eliminate transitional regulation can be easily adopted.

The rules on competition, and particularly those established in the EC Treaty might play an important role for the elimination of the negative effects of over-regulation. They have built in mechanisms for the evaluation of the competitive structure of markets that allow for the evaluation of whether effective competition has emerged in a de-monopolised market. Therefore, such mechanisms might allow defining the point in time in which transitory regulation for the promotion of competition is not necessary anymore.

Furthermore, the mechanisms for the control of State measures with anticompetitive effects allow Community authorities to overrule regulatory obligations with such an effect. Regulatory authorities are subject to significant pressures both from political authorities and from the regulated industry. At the same time, in markets with a complicated structure, regulatory authorities might just miss their point and introduce obligations, which not only do not foster competition but actively obstruct it. Competition Law has mechanisms to counterbalance such anticompetitive intervention.

106. Limitations of regulation. The most important limitation for regulatory intervention in the telecommunications markets is the respect for the free market mechanisms. The reform of the telecommunications sector has substituted direct public intervention by free market mechanisms as the main instrument ruling the sector. Regulatory intervention by the public authorities should not obstruct the regular functioning of such mechanisms, since such obstruction would impair the functioning of the fundamental mechanisms of organisation in the sector.

As it was observed earlier, one of the characteristics of regulatory intervention which was conclusive to its adoption in the field of telecommunications was its capacity to be developed in a competitive market without obstructing its regular functioning. This does not mean, nevertheless, that such compatibility is an intrinsic characteristic of regulatory intervention, as the American experience of regulation of the sector shows. It is for this reason that particular attention has to be devoted to the effects on the market of regulatory obligations imposed on the operators.

It is important to note at this point that Community authorities use mechanisms to outlaw regulatory interventions of the national authorities which obstruct competition in the liberalised markets. These are the same mechanisms which were used to abolish the exclusive rights granted for the exploitation of the telecommunications services and infrastructures. On the one hand, Community Directives, and particularly telecommunications harmonising Directives exclude certain regulatory measures of the Member States because of their obstructing nature. Article 169 EC Treaty could be used by Community authorities in order to abolish such actions. On the other hand, Community authorities can make use of Article 90 and of Articles 85 and 86 in relation to Article 5 EC Treaty in order to obstruct state measures with anticompetitive effects.

More concretely, regulatory intervention should not be unproportionate or discriminatory.[293] Obligations imposed on operators active in the markets should not be unproportionate, in the sense that the obligations imposed on them should not create such a burden as to obstruct their regular functioning. Connected to this limitation are the restrictions on public action imposed for

[293] Community Directives make continuous references to the limitations of State action. The main example can be found in the licenses Directive, where it is stated that "any conditions attached to authorisations should be objectively justified in relation to the service concerned and should be non-discriminatory, proportionate and transparent", paragraph 10 Directive 97/13/EC.

the respect of private property that exclude confiscatory measures. Discrimination is an important risk in the exercise of asymmetric regulation. The asymmetries in the obligations imposed on the operators according to their position in the market should be objectively justified, and should not impede a balanced competition in the market.

5.3.4. The Case of Price Control.

107. Anticompetitive pricing. Public intervention in relation to anticompetitive pricing provides a good model for the study of the interrelation between competition Law and economic regulation with regard to exclusionary practices by former monopolies.

The introduction of competition in the European telecommunications markets is forcing the former monopolists to reduce their prices in order to meet the competitive pressure of the new operators. Nevertheless, there is the risk that the pricing policy of the incumbents is not merely designed to meet competition but to eliminate it through the abuse of their market power. The incumbents can implement a policy of cross-subsidisation from those markets in which competition emerges slower (the local loop, for instance) to those markets in which competition is emerging faster (as long-distance telephony), in such a way that they can offer prices below costs which can exclude smaller competitors from the market.[294] This is especially possible if the incumbents maintain legal or factual monopolies in neighbouring markets. This behaviour is denominated predatory pricing.

In the US there has been a long debate on the application of the rules on competition for the obstruction of predatory pricing, steaming from an erratic

[294] LARSON & KOVACIC (1990): "Predatory Pricing Safeguards in Telecommunications Regulation: Removing Impediments to Competition", in *Saint Louis University Law Journal*, vol. 35, no. 1, p. 1.

case law[295]. The traditional position, fixed by Areeda and Turner[296], was that a price is predatory, and therefore contrary to the Sherman Act, if it is under the average variable cost. Nevertheless, subsequent literature and case-law[297] have toned down such position, as it has been demonstrated that it is possible to obtain exclusionary effects with prices over a certain level and that prices which fall under that level for short period of time might have an economic justification. The most radical literature has even suggested that there is no economic base for predatory pricing.

In the UE, from the ECJ judgement in *AKZO*[298], it is considered that a price is predatory, and therefore, prohibited by Article 82 EC Treaty, if it is below the average variable costs. Prices above such a level but below the average total costs (which include both variable and fixed costs) might also be prohibited if no objective economic justification can be proposed.

A number of European incumbents have been accused of breaching the competition Law prohibition of predatory pricing. Deutsche Telekom (DT) was accused before the European Commission for this reason at the beginning of 1996. DT finally retired the proposed pricing scheme, but Commission authorities made clear that "hasta que la liberalización completa sea conseguida, la Comisión debe prestar una atención particular a los efectos y motivaciones de las reformas tarifarias".[299]

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[295] GOMEZ SEGADE (1997): "*Precios predatorios y derecho antitrust*", Marcial Pons, Madrid.

[296] AREEDA & TURNER (1975): "Predatory Pricing and Related Practices Under Section 2 of the Sherman Act", in *Harvard Law Review*, vol. 88, pp. 697-733.

[297] Fundamental was *Matsushita Electronic Industry Co.* v. *Zenith Radio Corp.*, 475 U.S 574 (1986). For the subsequent evolution see AUSTIN, Page (1990): "Predatory Pricing Law since Matsushita", in *Antitrust Law Journal*, vol. 58, pp. 895-911.

[298] Case C-62/86, *AKZO Chemie v. Commission*, ECR [1991[2259.

[299] SCHAUB, A. (1996): "Competition Policy in the Telecoms Sector", in *Competition Policy Newsletter*, vol. 2, no. 1, p. 6.

Also in Spain Telefónica was accused of predatory pricing by British Telecom (BT). The *Servicio de Defensa de la Competencia* considered that Telefónica had incurred in such practices as regards the market of leased lines. The *Tribunal de Defensa de la Competencia* finally considered that the *Servicio* had not provided enough evidence as to impose a penalty, but recognised that the dominant position of Telefónica, its financial capacity and the particular structure of recently liberalised markets could make it economically beneficial for the incumbent to engage in such a behaviour.[300] Similar problems have been faced in the Netherlands and in Israel.

Competition Law, nevertheless, does not provide the only mechanisms to control such behaviour. Due to the particular characteristics of the telecommunications markets in the period of transition to effective competition, most Member States have defined price control mechanisms of a regulatory character. For instance, in Spain, national Legislation bestows on the Government, advised by the NRA, the power to control the prices of the operators (particularly of those with significant market power) through previously approved mechanisms or even through the definition of minimum prices of fixed prices. In this way, price schemes are controlled before they are implemented.[301]

As a result, in Spain, as in many other Member States, both mechanisms of intervention coexist. This coexistence was brought about by the need to effectively obstruct a behaviour which could seriously damage new comers. The long antitrust procedures might not be efficient enough in a period of transition in which market structure favours this kind of behaviour, and, at the

[300] Resolution of the *Tribunal de Defensa de la Competencia*, Case 412/1997, *BT* v *TELEFÓNICA*.

[301] In Spain even specific provisions have been introduced as regards the advertising of price schemes before they are approved, see MONTERO & BROKELMANN (1999): "*Telecomunicaciones y televisión. La nueva regulación en España*", Tirant lo Blanch, Valencia.

same time, it is not always simple to prove the existence of such an abusive practice.

However, regulatory intervention is prone to capture and to over extend the application of such intervention even after the disparition of the situation which gave rise to the creation of the regulatory mechanisms. For all these reasons, a counterbalanced intervention of the regulatory and the competition authorities can have beneficial effects.

Different reasons can take a regulator to accept prices which might have exclusionary effects. The review of their decisions by the competition authorities (national if granted such power, or Community authorities under the *effet outil* doctrine) might provide an efficient mechanisms to solve the problem. The case of DT's 1996 price scheme might be a good example of the positive effects of this counterbalanced approach. At the same time, competition authorities are in a good position to measure the need for such intervention as effective competition emerges in the telecommunications markets.

Both policies also face common problems. The main one is the difficulty in determining the cost of a particular cost in a network industry like telecommunications. Both competition authorities and regulatory authorities base their intervention with regard to prices on the relationship between prices and costs. The theoretical and practical difficulties in the determining costs advisees the collaboration between all the institutions for the development of efficient cost-determination systems.[302]

[302] *Vide infra* Chapter 9.2.3. Compulsory Access.

5.4. FROM REGULATION TO COMPETITION?

5.4.1. Public Intervention in Oligopolistic Markets.

108. From de-monopolisation to effective competition. It has been stated the scope of the liberalisation process has been the substitution of public monopolies through the pressure of effective competition on all market players. Public intervention was considered necessary in order to facilitate the emergence of effective competition, as otherwise there was the risk of creating private monopolies.

An analysis of the 1998 regulatory framework proves that public intervention for the promotion of the emergence of competition in the market was focused on the incumbents, and in particular in the management of their public telephony networks.

Public intervention was concentrated on the incumbents since they were initially the only operators with market power. These operators not only had the control of the only existing universal telecommunications network, but a market share in most service markets close to a 100%. The asymmetrical regulation created by the 1998 regulatory framework imposed obligations almost exclusively on the incumbents, as they were the only operator with widespread market power.

At the same time, the 1998 regulatory framework focused on those product markets which were more relevant at the moment the directives were adopted. As a result, only a limited number of telecommunications markets were considered, mostly public telephony network and services and leased lines. As a matter of fact, new markets such as mobile communications networks and services received very little attention. The reasons might be that these markets were not subject to exclusive and special rights, and also because their importance was not fully understood.

The 1998 regulatory framework not only focused on a very limited range of product markets and operators, it was not flexible with regard to the extension to new markets.

As a matter of fact, it was thought that the regulatory framework was of a transitory nature. As the market power of the incumbent would diminish as a result of the competition by new comers, the regulatory framework should be eliminated. The Directives did not include specific phase-out provisions, but defined clearly this principle.

The more traditional telecommunications markets (voice telephony and leased lines) have witnessed the entrance of new comers and a significant diminution of the incumbents market share in many market segments (backbone circuits and long distance telephony), even if local telephony and access lines have remained largely under the control of the incumbents.

In any case, and in particular with regard to network competition, it is possible to identify a tendency towards a not fully competitive market structure. The significant barriers to entry, the relevance of sunk costs, the economies of scale and scope etc. have limited market entrance and therefore given rise to a very concentrated market. Many markets are adopting a oligopolistic structure with a clear tendency for collusion.

109. New markets. As some competition has started to emerge in the traditional voice telephony markets, the telecommunications markets have witnessed the increasing relevance of new telecommunications networks and services. The most relevant case is, certainly, the wireless telephony markets. Examples are the digital TV networks, the IP networks and in general the Internet services.

For the most part, these markets have evolved in a liberalised environment in which special or exclusive right did not exist or had little relevance. Nevertheless, experience shows that such an evolution has not

always led to the emergence of effective competition. The aforementioned characteristics of network industries, and the identified principle of "winner takes it all" leads often to concentrated markets with a very rigid competition. The mobile telephony network market is probably the best example of the tendency of network industries to oligopolistic market structures. Digital TV networks, no matter whether by satellite, cable or terrestrial, also prove this tendency.

110. Oligopolistic markets. It is possible to argue that a significant share of both traditional and new telecommunications markets are adopting an oligopolistic structure. Actually, it was possible to foresee such an evolution of the telephony networks and other telecommunications market. Furthermore, this structure is not necessarily negative. Economic science proves that in theory, effective competition is possible not only in concentrated markets but even in duopoly markets.

The Bertrand price competition model proves that duopolists will experience effective pressures to price at marginal costs levels as whichever firm that offers the lower price in the market will monopolise the market. However, economic theory shows also that this equilibrium is only possible if sunk costs are literally zero. In case there are sunk costs, not matter how small, such costs become a barrier to entry and leads to competition to enter the market first. Since effective competition would lead prices to marginal costs, sunk costs would not be recovered, so the first comer achieves the protection of such a barrier to entry.

A similar problem is faced in oligopolistic markets. Competition is perfectly possible in theory, but the relevance of sunk costs in network industries, the homogeneous character of telecommunications services, and the low contestability of network markets (particularly if there is a physical barrier to entry as in mobile communications) are obstacles to competition. As a

matter of fact, competition in oligopoly markets with high sunk costs can only take place at the expense of the duplication of sunk costs. Such an equilibrium is reachable in repeated non-co-operative games given that the very same experience of market players makes the threat of a price war credible for all the players. Since cheating in the game involves a temporal gain in profits followed by a long-term loss, no firm ever wants to cheat if losses are bigger than gains. As a result, such a credible threat can enforce perfectly collusive outcomes for as long as technology does not evolve.

111. Concerted practices. The European rules on competition provide two different mechanisms against tacit co-ordination between oligopolists. Such co-ordination can be considered a concerted practice under Article 81 EC Treaty (or the correspondent national provision) or it can be considered an abuse of a collective dominance under Article 82.

Article 81 (former Article 85) prohibits "any agreement [...] or concerted practice [...] which has as its object or effect the prevention, restriction or distortion of competition". It is clear that Article 81 out-laws explicit agreements between oligopolists to reduce output and increase prices. The problem usually faced by competition authorities is to prove the existence of such explicit agreements. After decades of antitrust enforcement in Europe, companies are fully aware of the need not to produce any evidence which can be used by competition authorities to prove collusion. In this way, no written record of the agreement is produced, internal memoranda and even records of meetings between competitors are also avoided. Companies have become increasingly sophisticated as regards the mechanisms used to exchange information and to reach agreements.

Furthermore, in oligopolistic markets with a strong tendency towards tacit co-ordination (repeated game, price transparency etc.) it is not usually necessary to hold meetings in order to reach explicit agreements. Concerted

practices are usually enough to avoid the pressures of competition.[303] As it was put by the Commission "where related conduct by the parties did not result from an agreement that could be proved that conduct could nevertheless be viewed as constituting a concerted practice".[304] In repeated games, companies can just co-ordinate their behaviour as the game develops. Price transparency allows companies to adapt their behaviour to the competitors strategy. Companies can launch signals to their competitors and through these signals co-ordinate their strategies.

It is not simple for competition authorities to prove the existence of a concerted practice. Very little documentary evidence can be found in order to prove the existence of concerted practices (internal memoranda, for instance) but, once again, European companies have learnt not to produce or to eliminate such evidence. As a result, competition authorities can only rely on market analysis in order to prove, firstly, the existence of connection between the strategies of the competitors (even if it is clear that in markets with fierce competition companies react to competitors behaviours), and secondly the anticompetitive results of the connection in the companies strategies (reduction of output against consumer welfare, for instance).

It is clear that such economic analyses are highly sophisticated. The elaboration of such analyses requires significant resources which competition authorities do not always have at their disposal. At the same time, in case they are challenged, such analyses have to be backed by Courts which do not usually have the ability to judge them. As a consequence, competition authorities have been reluctant to rely exclusively on such analyses and usually

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[303] See ALESE, F. (1999): "The Economic theory of Non-Collusive oligopoly and the Concept of concerted practice Under Article 81", in *European Competition Law Review*, no. 7, pp. 379-383; and JONES, A. (1993): "Woodpulp: Concerted practice and/or conscious Parallelism?", in *European Competition Law Review*, p. 273.

[304] *Polypropylene*, Commission Decision 85/398/EEC [1986] OJ L 230/1, para . 4.

require some evidence or at least some strong presumptions in order to intervene against concerted practices.[305]

Even in those cases in which competition authorities have managed to identify collusive behaviours in oligopolistic markets and have fined the companies involved, such intervention does not ensure the end of such behaviours. The very same tendency of the markets has often lead to new collusive behaviours, of a more sophisticated nature, as companies have improved their ability to hide their strategies as a result of the intervention in the past of the competition authorities. As a matter of fact, competition authorities have concentrated most of their intervention in oligopolistic markets such as pharmaceuticals, concrete etc. but cannot claim to be fully effective.

Article 81 EC Treaty, thus, has not been an effective mechanism to obstruct the anticompetitive effects of concerted practices in oligopolistic markets.

112. Collective dominance. The European rules on competition provide a second instrument of intervention against anticompetitive behaviours in oligopolistic markets. Article 82 EC Treaty outlaws "any abuse by one of more undertakings of a dominant position".[306]

The limitations of Article 81 EC Treaty were always evident and as a consequence in the early 70s the Commission undertook the first attempts to make use of Article 82 against anticompetitive behaviours in oligopolistic

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[305] *Vide* ALESE (1999), p. 383 (*supra* footnote 303).

[306] See BRIONES, 1995): "Oligopolistic Dominance: is there a Common Approach in Different Jurisdictions?", in *European Competition Law Review*, p. 334; CAFFARRA, C. and KUHN, K. U. (1999): "Joint Dominance: The CFI Judgement on Gencor/Lonrho", in *European Competition Law Review*, no. 7, pp. 355-359; KORAH, V. (1999): "Gencor v. commission: Collective Dominance", in *European Competition Law Review*, no. 6, pp. 337-341; VENIT, 1998): "Two Steps Forward and No Steps back: Economic Analysis and Oligopolistic Dominance after Kali und Salz", in *Common Market Law Review*, vol. 35, p. 1101; WHISH, R. (2000): "Collective Dominance", in "*Liber Amicorum for Lord Slynn*", vol. 1; and WINKLER and HANSEN (1993): "Collective Dominance under the EC Merger Control Regulation", in *Common Market Law Review*, vol. 30, p. 787.

markets.[307] Nevertheless, the ECJ adopted a negative view against this trend, and in *Hoffman-La Roche* stated: "A dominant position must also be distinguished from parallel courses of conduct which are peculiar to oligopolies in that in an oligopoly the courses of conduct interact, while in the case of an undertaking occupying a dominant position the conduct of the undertaking which derives profits from that position is to a great extent determined unilaterally".[308] The Commission refrained then to make use of this strand.

Nevertheless, by the end of the 90's, the Commission made a new attempt to make use of Article 82 against anticompetitive oligopolies.[309] In this occasion, the CFI adopted a more positive attitude: "There is nothing, in principle, to prevent two or more independent economic entities from being, on a specific market, united by such economic links that, by virtue of that fact, together they hold a dominant position vis-à-vis the other operators on the same market."

Even if the CFI backed the possibility for two or more companies to enjoy a collective dominant position, the paragraph just quoted was interpreted in the sense that a particular economic link between the companies would be required in order apply Article 82. The CFI did not specify what kind of economic link. It proposed some examples (as intellectual property licences) but it did not clarify whether the mere oligopolistic structure of the market would be considered a sufficient economic link between the competitors. This doubt has not been further clarified by the CFI nor the ECJ.[310]

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[307] See for instance COM(1975) 675, "Report on the Behaviour of the Oil Companies during the period from October 1973 to March 1974", 10.12.1975; *Sugar Cartel*, Commission Decision 73/109/EEC OJ [1973] L 140/17.

[308] See Case 85/76, *Hoffmann-La Roche v. Commission* [1979] ECR 461, para. 39.

[309] *Italian Flat Glass*, Commission Decision 89/93/EEC OJ [1989] L 33/40.

[310] Case C-393/92, *Almelo v. NV Energiebedrif Ijsselmij* [1994] ECR I-1477; Case C-96/94, *Centro Servizi Spediporto Srl v. Spedizioni Maritime del Golfo Srl*, [1995] ECR I-2883.

The Commission, in any case, went forward and adopted a series of decisions based on the collective dominance doctrine.[311] Furthermore, the Commission's position as regards the nature of the economic links which should create the collective dominance was clarified in the Access Notice: It is a sufficient economic link if there is the kind of interdependence which often comes about in oligopolistic situations. There does not seem to be any reason in law or in economic theory to require any other economic link between jointly dominant companies".[312]

The doubts were cleared by the CFI in *Gencor v. Commission*. In this judgement, the CFI clearly stated that in its Judgement in the *Flat Glass* case, the Court referred to links of a structural nature only by way of example and did not lay down that such links must exist in order for a finding of collective dominance to be made". "Furthermore, there is no reason whatsoever in legal or economic terms to exclude from the notion of economic links the relationship of interdependence existing between the parties to a tight oligopoly within which, in a market with the appropriate characteristics, in particular in terms of market concentration, transparency and produce homogeneity, those parties are in a position to anticipate one another's behaviour and are therefore strongly encouraged to align their conduct on the market, in particular in such a way as to maximise their joint profits by restricting production with a view to increasing prices. In such a context, each trader is aware that highly competitive action on its part designed to increase its market share (for example a price cut) would provoke identical action by the others, so that it

[311] *French-West African Shipowners' Committees*, Commission Decision 92/262/EEC OJ [1992] L 134/1; *Cewal*, Commission Decision 93/82/EEC OJ [1993] L 34/2: *Port of Rodby*, Commission Decision 94/119/EC OJ [1994] L 55/52; and *Irish Sugar*, Commission Decision 97/624/EC OJ [1997] L 258/1.

[312] *Vide* Access Notice, para. 79 (*supra* footnote 265).

would derive no benefit from its initiative. All the traders would thus be affected by the reduction in price levels".[313]

This Judgement was followed by a number of relevant Commission decisions such as *Price Waterhouse/Coopers & Lybrand*,[314] and *Aitours/first Choice*.[315] It is important to point that all these cases resulted from the application of the Merger Regulation and not as a result of the application of Article 82.

It might not be simple to expand the application of the case-law on collective dominance from merger cases to Article 82 cases, particularly to exploitative abuses.[316] It has already been shown that the rules on competition are particularly strict against market power when such a situation would be reached by a merger. It is not clear if a similarly strict approach could be developed by the competition authorities against collective dominance positions already present in the market.

In particular, it is not clear whether the Commission could impose a price reduction based on the findings that, without any collusion, not even parallel behaviour, merely as a result of the very same market structure, collectively dominant undertakings are imposing excessive prices. It seems clear that in case there is collusion or concerted practices, actions have to be brought based on Article 81 and not Article 82. If this is not the case, the Commission would have to intervene in order to impose a price different from the price derived from the rational behaviour of market players. Once more, the Commission would adopt a regulatory approach. More clear is the possibility for the

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[313] *Gencor v. Commission*, Case T-102/96 [1999] ECR 4, para. 273 and 277.

[314] *Price Waterhouse/Coopers & Lybrand*, Case IV/M. 938 OJ [1997] L 50/27.

[315] *Aitours/First Choice*, Case IV/M. 1524.

[316] *Vide* WHISH (2000), (*supra* footnote 306).

competition authorities to proscribe exclusionary practices by collectively dominant players.

113. Antitrust and collective dominance in telecoms. It has been shown that many telecommunications markets, particularly network markets both traditional and newer, have a strong tendency to adopt an oligopolistic structure with tacit co-ordination. Some fundamental features of telecommunications markets (concentration, price transparency, relevance of sunk costs, relevance of barriers to entry etc.). As a matter of fact, the Commission has recognised this tendency in the Access Notice,[317] as even interconnection agreements might create economic links which would facilitate collusion.

Experience proves that the rules on competition have never been effective in order to exclude distortions in collusive oligopolies. The new collective dominance approach to collusive dominance might provide some sharper tools for intervention, but such intervention risks denaturalising antitrust and once more strengthening its regulatory tendency.

114. Economic regulation and collective dominance. The Commission seems aware of this risk and for this reason might have decided to complement antitrust with sector specific instruments. As a result of the 99 Review, the Commission has recognised that sector specific regulation is still necessary, as effective competition might not emerge in all the telecommunications markets, and competition law remedies might not be sufficient to address the problems.[318]

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[317] *Vide* Access Notice para. 79 (*supra* footnote 265).

[318] See COM(2000) 393, Proposal for a Directive of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services, of 12.07.2000, para 21.

As the Commission proposes to extend the antitrust dominance test to the regulatory arena, it has proposed to impose the regulatory framework not only on those operators individually holding a dominant position (mostly the incumbents) but also on operators jointly holding such position: "An undertaking shall be deemed to have significant market power if, either individually or jointly with others, it enjoys a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers".[319]

We have already pointed to the problems raised for the use of the antitrust dominance category in the regulatory field. The transplant of the collective dominance test to this field might entail further problems. The Commission proposes to raise the thresholds for intervention from a mere 25% market share to an antitrust dominance test. The collective dominance doctrine is suppose to allow the regulatory authorities to intervene in oligopolistic markets without a clear market leader. The problem is that in case the European Courts change their tendency and dismiss the collective dominance doctrine, and the weaknesses of the doctrine does not make this impossible, public intervention both antitrust and regulatory, would be impossible despite the evident distortions in the market.

5.4.2. Regulation and the General Interest.

115. General interest objectives outside of the scope of the market. Competition Law can promote the efficiency in the market, but it is clear that certain general interest objectives fixed by public authorities are outside of the reach of the operators active in the market. The provision of certain basic

[319] *Ibid.* Article 13(2).

services at an affordable price, for instance, might require the definition of prices below cost.

Even if competitive structures reinforced by a strict application of the rules on competition, can promote efficiency and lower costs, after a certain limit, another instrument of public intervention (public subsidies, the creation of a fund for the financing of the provision of the service below cost etc.) will be required for the fulfilment of the general interest objective.

116. Regulation and other general interest objectives. Even in case liberalisation produces an increase in the efficiency of the telecommunications operators, reduces prices and ameliorates the quality of the telecommunications services, as pled by the defendants of the process of reform of the sector, it is widely recognised that some objectives of general interest will, in all likelihood, not be ensured by the mere interaction of the mechanisms of supply and demand in a competitive market. There are general interest values that are out of the scope of the market. It does not mean that such objectives are incompatible with the market, but rather, that they are not necessarily among the results of effective competition. In these cases, the application of competition Law does not ensure either the satisfaction of the general interest, since such an instrument only protects the market mechanisms and cannot guarantee the fulfilment of objectives foreign to the market's logic.

Community authorities and in general the defendants of the process of liberalisation have been accused of scorning the satisfaction of general interests outside the scope of the market, as well as of eliminating all the elements of solidarity that have traditionally ruled the provision by the national monopolies of the public utilities in Europe. Nevertheless, it has to be argued that the reform of the telecommunications legislation has not eliminated all the instruments of public intervention in the defence of the general interest but has merely substituted the traditional direct intervention instruments, incompatible

with the new competitive structure, with new instruments of indirect public intervention. This substitution has facilitated the transformation of the political responsibility of the public authorities in the provision of the services of general interest, in legal responsibilities bestowed in the private providers of the services, but also in the public authorities, in such a way that for the first time, citizens have the legal right to enforce the satisfaction of the general interest.

The obligations imposed on the operators should not obstruct the regular functioning of the competitive mechanisms of the market. At the same time, the obligation imposed on the operators cannot create for them an excessive economic burden, as this would amount to an illegitimate confiscation. As a result, mechanisms of distribution of the economic burden of the obligations imposed on the operators have been defined at a Community level, among them the Universal Service Fund.[320]

5.5. CONCLUSIONS.

117. Final. When it was decided to de-monopolise European telecommunications markets, it was commonly understood that public intervention would be necessary in order to facilitate the transition from public monopolies to effective competition.

The rules on competition proscribed the behaviour of incumbents trying to prevent the emergence of competition, and at the same time, provided some instruments to proscribe exploitative abuses by the incumbents. Nevertheless, it was understood that the rules on competition would not be enough to foster competition and ensure the satisfaction of the general interest.

[320] *Vide infra* 9.3. Regulating Access by Consumers.

On the one hand, the European rules on competition were designed to defend existing competition and to eliminate behavioural obstacles to the emergence of new competition in the market. Nevertheless, such rules are not fitted to reduce or eliminate the structural obstacles to competition derived from the very same presence in the telecommunications markets of the incumbents. These operators benefit from the economies of scale and network externality effects which characterise network industries.

At the same time, even if the antitrust rules can guarantee the orientation of prices to costs and some cost reduction as a result of the constraints of competition, it is clear that these rules can never guarantee the provision of services below costs in order to fulfill general interest objective.

As a result of the limitations faced by antitrust, sector specific regulation was introduced by European authorities. Such regulation was focused, on the one hand on access to the incumbents' more traditional telephony networks and leased lines. This intervention was considered transitory, as it was supposed to disappear with the emergence of effective competition. On the other hand, obligations on universal service were introduced.

Nevertheless, the tendency to collusive oligopolistic market structures both in the more traditional markets (telephony networks) and in new markets (mobile communications, digital TV networks) might entail the necessity of maintaining certain regulatory obligations on operators enjoying market power, whether exclusively or jointly with other competitors. This intervention is certainly subsidiary. If competition emerges, it should be eliminated, but this might not be the case, as market failures might be of a permanent or at least stable nature.

CHAPTER 6

INSTITUTIONAL FRAMEWORK

SUMMARY: 6.1. Introduction. 6.2. Concentrated Structures. 6.3. Dual Structures. 6.4. Conclusions.

6.1. INTRODUCTION.

6.1.1. Competition and Regulatory Authorities.

118. General. The existence of two main instruments of public intervention in de-monopolised markets has determined the institutional framework for public intervention in de-monopolised markets.[321] In most of the industrialised States, specialised institutions (National Competition Authorities NCAs) enforce the general rules on competition even if in connection with

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[321] For an analysis on the influence of the institutional framework in the liberalisation process see SCOTT, C. (1996): Institutional Competition and Co-ordination in the Process of Telecommunications Liberalisation", in "*International Regulatory Competition and Co-ordination*", Claredon Press, Oxford, pp. 381-413.

other national institutions (as the judiciary or regional authorities in federal states) and with supra-national institutions in the case of the Member States of the European Union. At the same time, the liberalisation of the telecommunications markets has fostered the creation of sector specific institutions in many States where such institution did not exist before. The structure, legal status and competencies of such National Regulatory Authorities (NRAs) are very varied.

The distribution of competencies between the competition authorities and the regulatory authorities is complicated by the fact that most of the NRAs have as an explicit or implicit goal the promotion of competition in the telecommunications markets. Even if most of the NRAs are not competent to enforce the rules on competition, some of the NRAs have interpreted in a very broad sense the competencies they enjoy for the promotion of competition, and this has created conflicts with the competition authorities.

The competition between different authorities for the provision of the best solutions for the actors in the market can have interesting beneficial effects, as long as the distribution of competencies between the institutions is clear and the authorities involved in such competition are not tempted to pass certain basic limits in order to obtain "clients".

The problem of the incompatibility of policies is also important. Even if the NRAs have as their main objective the promotion of competition, in some cases they might be tempted to adopt their own strategy to reach such an objective, through the over-regulation of the markets. Furthermore, they can even adopt anticompetitive measures (for example in relation to universal service).

The most radical solution for such conflicts has been to avoid the creation of two different institutions, and the concentration of both the antitrust and the regulatory powers in a single institution. In such a way, antitrust authorities

have been granted regulatory powers in de-monopolised markets for example in Australia. Contrariously, it has been a common request by the regulatory authorities to enjoy an exclusive application the rules on competition in the regulated sector, excluding the intervention of the national competition authority in such markets.

In those cases in which two different institutions intervene in the de-monopolised markets, it has been common to establish a static distribution of competencies, and to leave for the institutions to reach an equilibrium through confrontation and informal agreements. Nevertheless there are interesting examples of more dynamic approaches which try to create formal and transparent mechanisms of co-ordination between the competition and the regulatory authorities for the definition of the borderline between both kinds of intervention.

119. Competition authorities. The institutional framework for the application of competition Law in Europe has a more solid tradition than the regulatory institutional framework. This does not mean, however, that such a framework is characterised by its clarity and simplicity. The framework is complicated by the coexistence of two sets of rules: on the one hand the Community competition Law, and on the other the national competition Law (usually designed following the structure of Community competition Law), and the necessary co-ordination between both the sets of rules and the institutions which apply them.

Community competition Law is centrally applied by Directorate General IV of the European Commission. At the same time, some of the rules contained in the EC Treaty are directly applicable and therefore can be applied by the national judiciary. Even more, some Member States have empowered the

national competition authorities to apply Community competition Law.[322] Regulation 17/62 creates some mechanisms of co-ordination between the Community and the national competition authorities, and the trend is towards the de-centralisation of the application of the Community rules on competition.[323] Such a trend coexists with the proposal for the creation of an independent agency (a European Cartel Office) in charge of the application of European competition Law, in the framework of the European Union, in order to increase the efficiency of it application and to reduce political interference.[324]

Over the decades, member States have all developed their own set of rules on competition and in parallel have established specific institutions for the application of such rules (and in some cases also of the Community rules on competition). National competition authorities (NCAs) have different legal status, even if there is a general tendency for them to enjoy a certain degree of independence from the general administration. The specificity of the rules on competition and their complexity has often recommended such separation and the establishment of specific institutions with their own administrative procedures.[325]

120. Regulatory authorities. The first regulatory authorities appeared in the US by the turn of the century. Their raison d'etre was the development of regulatory intervention in markets of general interest. In the framework of the extension of public intervention in the economic activity during the New Deal

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[322] See EHLERMANN, C. D. (1996): "Implementation of EC Competition Law by national antitrust authorities", in *European Competition Law Review*, no. 2, p. 88.

[323] See EHLERMANN, C. D. and LAUDATI, L. Ed. (1997): "*Annual on European Competition Law 1996*", Kluwer, The Hague.

[324] EHLERMANN, C. D. (1995): "Reflections on a European Cartel office", in *Common Market Law Review*, vol. 32, p. 471.

[325] For the Spanish experience see BAÑO LEÓN, J. (1996): "El Servicio de Defensa de la Competencia y el Tribunal de Defensa de la Competencia: funciones y procedimiento", in "*La intervención administrativa en la economía*", CGPJ, Madrid, pp. 213-248.

period, the Federal Communications Commission (FCC) was created.[326] The establishment of the FCC was the culmination of the process of monopolisation of the American telecommunications markets. It developed a market substitutive intervention for decades, until the process of deregulation was initiated in the 70's.[327]

The recent creation of the regulatory authorities in the European Union, on the contrary, can only be understood in the framework of the process of liberalisation of the markets. Since the first steps of such process, it appeared indispensable to separate the management of the services by the Telecommunications Organisations (often in hands of the State), from the regulation of such markets, through the creation of regulatory authorities, independent from the Telecommunications Organisation[328].

The Community legislative framework contains numerous provisions in relation to the separation between management and regulation. The first reference was included in Article 6 of the Terminals Directive, which imposes upon Member States the obligation to ensure that the responsibility for drawing up technical specifications and granting type-approval would be entrusted to a body independent from public or private undertakings offering goods or services in the telecommunications sector. Such provision was later developed so as to ensure that national regulatory authorities would be legally distinct from and functionally independent from all organisations providing telecommunications networks, equipment or services.[329] The new directives

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[326] *Vide supra* Chapter 2.1. Origins and Evolution of Economic Regulation, and Chapter 2.4.2. The Regulated Monopoly, as well as MONTERO PASCUAL, J. J. (1996): "Titularidad privada de los servicios de interés general", in *Revista Española de Derecho Administrativo*, vol. 92, p. 590.

[327] See BROCK, G. (1981): "*The Telecommunications Industry. The Dynamics of Market Structure*", Harvard University Press, Cambridge MA.

[328] See, for instance, COM(87) 290 final, Green paper on Telecommunications, p. 15.

[329] Article 5a Directive 90/387/EEC as modified by Directive 97/51/EC, Article 7 Directive 90/388/EEC as amended by Directive 96/19/EC, and Article 2 Directive 97/13/EC.

proposed by the Commission as a result of the 99 Review reinforce the independence of the NRAs.[330]

The Community legal framework imposed as obligation ensuring the formal and substantive independence of the regulators from the operators. As most of the incumbent operators were directly or indirectly controlled by the public authorities, Member States had to develop mechanisms to ensure the independence of the regulator from other public authorities. As a result, most of the Member States created sector specific institutions independent from the rest of the executive branch.

Independent agencies had a long tradition in the US, as most regulatory agencies had this legal status. Nevertheless, independent agencies were not unknown in Europe, since a numerous of Member States had in the last decades developed a number of independent administrations aimed at excluding partisan decision-making in relation to delicate issues.[331] The list of European independent administrations, initially including administration with a guarantee function, has been increased with a new set of administrations with a regulatory function.

Just as independent agencies have created a long-lasting constitutional debate in the US, independent administrations have raised an interesting debate in the Member States, particularly in those States with a parliamentary system

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[330] "There was general support for the Review Communication's proposals to strengthen the independence of NRAs and to improve transparency of their decision-making. As has already been mentioned, many commentators called for increased co-operation with competition authorities and with the Commission.", in COM(2000) 239 final, Communication from the Commission , The results of the public consultation on the 1999 Communications Review and Orientations for the new Regulatory Framework, Brussels. The particular measures can be found in COM(2000) 393, Proposal for a Directive of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services, 12.7.2000, Brussels.

[331] The best example of this policy was the creation of independent administrations in France, Italy and other Member States for the control of broadcasting.

following Rousseau's model,[332] and a strong centralised administration as France or Spain.[333] Many European constitutions explicitly state that the Administration is under the control of the Government, which is directly responsible under the Legislative power Therefore, the creation of an independent administration, out-side the direct control of the Government and the indirect control of the Parliament supposes a radical exception to the general principles established in the constitution.[334]

Regulation by independent administration favours both specialisation and the full exploitation of the new mechanisms of public intervention offered by economic regulation. This is because a new administration can more easily adapt the traditional rules on administrative procedure to the new requirements of regulatory intervention, and in general to the new challenges of this new instrument of public intervention. Nevertheless, regulation by independent administration and not by the traditional administration has also disadvantages. The introduction of partisan politics in the functioning of the regulators would easily produce unbalances as power would be exercised with less rigid controls than usual, as political control would mostly be eliminated in favour of a

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[332] As it has been appointed by different authorors, independent administrations are closer to the Anglo-Saxon constitutional tradition derived from Locke's construction, that in the continental tradition of centralised napoleonic administration in the framework of Rousseaus's division of powers. See AMATO, G. (1997): "Autorità semi-independenti ed autorità di garanzia", en *Rivista Trimestrale di Diritto Pubblico*, no. 3, pp. 645-664.

[333] The French experience can be studied in COLLIARD and TIMSIT (1988): "*Les autorités administratives indépendantes*", PUF, Paris; and GUEDON, M. J. (1991): "*Les autorités administratives indépendantes*", LGDJ, Paris. Such experience had a strong influence in Italy and Spain. For the Italian case see PASSARO, M. (1996): "*Le Amministrazioni independenti*", Giappichelli, Torino. For the Spanish experience, see BETANCOR RODRÍGUEZ, A. (1995): "*Las Administraciones independientes*", Tecnos, Madrid; FERNÁNDEZ RODRÍGUEZ, T. (1994): "Reflexiones sobre las llamadas autoridades administrativas independientes", en "*Libro homenaje a Manuel Clavero Arévalo*", Cívitas, Madrid, pp. 427-439; and PARADA VÁZQUEZ, J. R. (1994): "Las administraciones independientes", in "*Libro homenaje a Manuel Clavero Arévalo*", Cívitas, Madrid, pp. 653-689.

[334] It is for this reason that in France, the competent Ministry has to confirm most of the decisions adopted by the regulatory authority in the telecoms sector (ART) following the Decision of the *Conseil d'État* n 88-248 DC January 17, 1989. In Spain such a solution has not been implemented, but the national regulatory authority (CMT) is formally attached to the Ministry of public works, even if there is no hierarchical relation between both institutions.

necessarily limited judicial review. At the same time, the regulatory administration could also be "captured" more easily by the industry, due to the closeness and even potential identification between the specialised administration and the regulated companies, particularly the new entrants.

As the process of liberalisation of the telecommunications operators reaches its conclusion, the need for independent regulatory administrations will be reduced. The obligation imposed on the Member States to separate formally the regulator from the rest of the administration will disappear as Member States complete the privatisation of the telecom operators. A tendency for regulatory mechanisms to become more and more common con be envisaged, in such a way that the traditional administration might tend to reduce its opposition to use them, and, furthermore, as effective competition emerges in the telecoms markets, regulatory intervention for the promotion of competition will be unnecessary.

The structure, competencies and powers of the national regulatory authorities are very different in the Member States, even if a few common characteristics can be defined. With regard to the structure of the regulatory administrations, most of the Member States have a dual structure, with a division of regulatory competencies between an independent regulatory administration and the competent Ministry. The degree of independence of the regulatory administration and the competencies bestowed to it vary from country to country. The very same structure of the independent administration varies, as some of them are unipersonal (UK and Sweden, for example) and other are collegiate (the number of members is also very variable). Even if it is common to have a reduced number of members in the executive council, (around 5), a number of examples of bodies with more members can be found.

The methods of the appointment of members are also different. Most of the Member States have balanced the lack of control by the Legislative by

ensuring an important role to the parliament in the appointment of the members. Nevertheless, this is not always the case, and sometimes the appointment is made by the Executive with little or no intervention by the Legislative (this is the case of Spain, for example). A fundamental mechanism for ensuring independence is the lack of a hierarchical relation between the independent regulatory administration and the government. Other mechanisms are the limitations to dismiss the members of the NRA, the limitations to re-eligibility, and the provision of sufficient economic and personal resources to the NRA.

With regard to the competencies of the independent regulatory authorities, it is common for them to enjoy competencies in relation to interconnection, numbering and universal service. In some cases, the competent Ministry maintains important competencies in the licensing procedures (this is the case of France and Spain, for instance). The same can be said about the management of radiolectric frequencies.

Powers are also unevenly distributed among the different national independent regulatory authorities. They usually enjoy executive powers for the application of the relevant legislation through legal measures affecting individual operators, as well as competencies for the resolution of conflicts between operators, with regards to, for instance, interconnection, the imposition of financial penalties and the withdrawal of licenses. Many of these powers involve a distributory activity of a quasi-judicial character, but the implementation of the procedures defined in the community directives has led Member States to grant such powers to the NRA.

More complicated has been the granting of normative powers to some of the national independent regulatory authorities. The power of implementing existing legislation through administrative acts of a general nature is usually reserved for the government under the control of Parliament. The exercise of

normative powers by the independent regulatory administrations, often appointed exclusively by Government, creates a constitutional conflict which is difficult to solve in favour of the NRAs. The limitation of such normative powers to the adoption of regulatory provisions, that is, of provisions of a general nature which merely implement existing rules adopted by the Legislator or by government, adapting its content to the specific conditions in the market of a specific category of operators could solve the conflict.[335]

Most of the competencies and powers granted to the NRAs are directly connected to what is defined as their main objective and the reason for their existence: the promotion of effective competition in the telecommunications markets. Even if this is the *raisson d'être* of most of the NRAs, it is not common for them to enjoy the competence to enforce the rules on competition, neither the community rules, nor the national rules.[336] On the contrary, different regulatory mechanisms have been defined (often by the Community Directives) for the attainment of such a result.

In some countries, important conflicts are arising in respect of the distribution of the competencies for the application of the rules on competition between the NCAs and the NRAs. Nevertheless, it is more common a conflict between authorities with regard to the co-ordination of the rules on competition applied by the NCAs and the regulatory mechanisms implemented by the NRAs.

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[335] See MONTERO, J. J. and BROKELMANN, H. (1999): "*Telecomunicaciones y televisión. La nueva regulación en España*", Tirant lo Blanch, Valencia, pp. 143-146.

[336] The British and the Greek cases are the most relevant exceptions to this general tendency.

6.1.2. The European Regulatory Authority.

121. The need for a European Authority. The proposals for the creation of a European Regulatory Authority[337] are as old as the involvement of the EC authorities in the telecommunications sector. As early as 1983 the Commission proposed the gradual transfer of national competencies on telecommunications to the European Community, and the creation of a European telecommunications agency.[338] The same proposal was launched in the Bangemann Report,[339] received by the Commission[340], and commented by different institutions and actors in the market.[341] As established in recital 25 of Directive 97/33/EC, in the framework of the 1999 Review it would be evaluated "the case for the establishment of a European Regulatory Authority, taking into account *inter alia* the preparatory work undertaken by the Commission".

The preparatory work by the Commission[342] showed some support for the assignation of some competencies to a European institution, mostly in relation to certain aspects of interconnection, numbering and licensing with a supranational content. Another issue was the specific articulation of the institutional solution for the development of such competencies. It was pointed

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[337] See SAUTER, W. (1994): "The ONP Framework: Towards s European Telecommunications Agency", in *Utilities Law Review*, vol. 5, pp. 140-146.

[338] COM(83) 329 final Communication from the Commission to the Council on Telecommunications, of 9 June 1983, p. 12.

[339] "*Europe and the global information society*". Recommendations to the European Council", 26 may, 1994.

[340] COM(95) 158 Communication from the Commission to the European Parliament and the Council. The Consultation on the Green Paper on the Liberalisation of telecommunications Infrastructure and Cable Television networks, 3 May 1995.

[341] See Forrester Norall & Sutton (1996): "*The Institutional Framework for the Regulation of telecommunications and the Application of the EC Competition Rules*", Report for the European Commission, Brussels, pp. 51 82.

[342] See NERA (1997): "*Issues Associated with the Creation of a European Regulatory Authority for Telecommunications*", Report for DG XIII European Commission, Brussels; and CULLEN & EUROSTRATEGIES (1999): "*The Possible Added Value of European Regulatory Authority for Telecommunications*", Report for DG XIII European Commission, Brussels.

out that the exercise of such competencies at an European level would not require the creation of an specific independent agency in the framework of the European Union, but a mere assignation of competencies to the existing services of the Commission, or even the recognition of a role of co-ordination of the different NRAs could be enough. In the case where it was considered that an independent agency was necessary, one of the main debates would be the transfer or the delegation of the Commission's power to apply the community rules on competition to such agency.

122. The new institutional framework. As a result of the broad consultation, the Commission decided not to propose the creation of an European Regulatory Authority, but rather to strengthen the actual framework: "The Commission considers at this stage that the creation of an European Regulatory Authority would not provide sufficient added value to justify likely costs. In addition, it could lead to duplication of responsibilities, resulting in more rather than less regulation. The issues identified that might be better dealt with at EU level can be addressed through adaptation and improvement of existing structures".[343]

As a matter of fact, the Commission has finally proposed the substitution of the ONP Committee and the Licensing Committee by the COCOM, the Communication Commission. This new entity should provide a framework both for operators and other private entities and Member States, to collaborate with the Commission.[344]

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[343] COM(1999) 539, Communication to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions reviews recent developments in the market for electronic communications services within the EU and provides a number of proposals for possible future regulatory measures specific to this sector, Brussels.

[344] See the specific proposal in COM(2000) 393, Proposal for a Directive of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services, 12.7.2000, Brussels.

6.2. CONCENTRATED STRUCTURES.

123. General. The coexistence of two different instruments of public intervention in de-monopolised markets does not necessarily mean the attribution of the competence to develop each different instrument by different institutions, and therefore the coexistence of two different institutions. On the contrary, different actors have pled for the convergence of the different instruments of intervention in a single institution.

The concentration of both instruments of public intervention in a single institution can have beneficial effects. It ensures a better co-ordination of the different mechanisms of public intervention, their complementarity and an increase in the efficiency of the intervention. On the contrary, it also entails risks. One of the instruments could remain underdeveloped in favour of the other one, and both could be de-naturalised, as the influence of the other could loose the perspective of the basic objectives and principles ruling each kind of intervention.

Two different models of concentration have been proposed. On the one hand, regulatory powers can be granted to the competition authorities, expanding their traditional power to apply the rules on competition in order to allow them to promote the very same creation of such competition in the de-monopolised markets, and to control the potential abusive behaviours during the transition from monopoly to competition. On the other hand, it has been proposed to grant powers for the application of the rules on competition to the sector specific regulatory authorities. In such a way, Competition Law would become another mechanism at the disposal of the regulatory authorities for the promotion of competition in the liberalised markets.

124. Concentration of powers in the hands of the NCAs. The most successful attempts to concentrate diverse powers of intervention in a single

authority have consisted in the assignation to the competition authorities of regulatory powers. It is widely understood that most of the regulatory mechanisms of intervention have a transitory nature, as they are designed for the period of transition from monopoly to competition.[345] Therefore, it can be considered more reasonable to bestow such transitory powers to the institution which will survive the transitory period, than to create a specific institution (taking into account the tendency of any institution to survive and expand its role). At the same time, competition authorities have a tradition of pro-competitive intervention which regulators have to build. The attribution of regulatory powers to the competition authority reduces the risk of capture of a sector specific regulator by the regulated industry, as the competition authorities would not have the tendency to assimilate itself with the industry, as it usually happens with the sector specific regulators.

The attribution of regulatory powers to the competition authorities could also have negative effects. Firstly, a horizontal institution could not develop a profound knowledge about a specific sector, knowledge that is necessary in order to develop a more intrusive intervention than antitrust in sectors characterised by their complexity. Secondly, there is the risk of an under-development of the regulatory mechanisms in States with little indirect intervention tradition. Regulatory instruments are foreign mostly to States with an interventionist tradition of direct provision of services through public companies.

As a result, in such countries, competition authorities could be tempted to renounce to the employment of their limited resources for the development of the regulatory mechanisms, and to expand the role of the antitrust mechanisms.

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[345] Even a partly as little suspectful as the French Secretary of Industry has recognised that the NCAs will survive the NRAs, even if he has pointed that the question is when such concentration will take place. see LASSERRE, B. (2000): "Competition or Regulatory Authorities? European or national

Lastly, such a solution could not only suppose the use of competition Law in order to obtain objectives which are foreign to its scope, but also to introduce some regulatory elements in the application of the rules on competition. In both cases, there is a high risk of de-naturalisation of the rules on competition.

The best example of the attribution of regulatory powers to a competition authority can be found in the Australian experience.[346] In this country, a strategy to expand the competencies of the competition authority from the narrow application of the rules on competition to the development of a much wider competition policy, has been pursued. This strategy has supposed the attribution of regulatory competencies to the competition authority, and the limitation of the development of sector specific regulatory authorities, which are limited to strictly technical intervention (management of radioelectric frequencies, etc.).[347]

In Australia, the regulatory competencies already granted to a sector specific regulator, Austel, for the promotion of competition, were taken over by the Australian Competition and Consumer Commission by the beginning of 1997. The remaining technical competencies were absorbed by a wider body covering telecommunications and broadcasting.

The main regulatory competencies of the competition authority are the review and reform of anticompetitive provisions adopted by the federal or the state governments, the review and reform of public monopolies, the restriction of monopoly pricing behaviour, the promotion of neutrality in the allocation of scarce resources, and the provision of third party access to essential facilities.

Level?", in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gossling Ed., Hart, pp. 629-636.

[346] The Danish institutional solution is also interesting.

[347] For an analysis of the Australian experience see FELS, A. (1997): "Decision making at the centre", in *Annual on European Competition Law 1996*", Ehlermann and Laudaty coord., Kluwer, The Hague.

Specific rules on access to essential facilities of a regulatory nature were adopted in order to complement the weaknesses of the rules on competition.[348] These rules contain provisions concerning the administrative procedures for the declaration of a facility as essential, for the arbitration in case of lack of agreement on the terms of access, and for the appeals. At the same time, the basic principles ruling the decision making are also defined. The introduction of substantial as well as procedural rules enhances legal certainty in the public intervention, what improves the solution of conflicts and obstructs the mixture between competition and regulatory intervention.

125. Concentration of powers in the hands of the NRAs. Less successful, but also active, have been the defendants of the concentration of both regulatory and competition powers in the hands of the regulatory authorities.

Their main argument is that the application of the rules on competition in such a complex sector requires a very detailed knowledge of the technicalities and the specific market structure and tendencies of the telecommunications sector. At the same time, co-ordination between regulatory and competition intervention would be enhanced by such an institutional solution. On the other hand, it has been sustained that it is just as difficult for the sector specific authorities to get acquainted with the complex rules on competition as it is for competition authorities to get acquainted with the telecommunications sector. Even more, this institutional solution would facilitate the development of a different application of the rules on competition, a sector specific competition Law, which would first of all complicate the future convergence with the general application of such rules once the transitory period is finished, and in any case, damage legal certainty.

[348] See PENGILLEY, W. (1998): "Access to essential facilities: a unique antitrust experiment in Australia", in *The Antitrust Bulletin*, vol. 43, no. 2, pp. 519-545.

National Regulatory Authorities have been actively trying to have these competencies granted by the national Legislators. In the case of Spain, for instance, different proposals were launched by minority parties in the parliamentary procedure for the adoption of the General Telecommunications Act, but such proposals were never successful. Nevertheless, the Spanish NRA has pursued a very aggressive policy, based on a doubtful interpretation of the existing legislation, consisting in the gradual adoption of such powers through case-by-case decision. For instance, they created a conflict with the European Commission when they publicly demanded to be informed of the competition procedures developed by DG IV according to the rights recognised to national competition authorities by Regulation 17/62.[349]

The option to grant powers for the application of the rules on competition to the National Regulatory Authorities was initially successful in Italy. The Italian Antitrust Act of 1990 expressly excluded the application of such rules by the antitrust authority it created in some specific sectors, including broadcasting.[350] Nevertheless, the application of the rules on competition was returned to the competition authority both in the Act which defined the general principles ruling public utilities (Act 481/1995) and the specific act which governs telecommunications and the Italian NRA (Act 249/1997).[351]

[349] *Vide* MONTERO and BROKELMANN (1999), pp. 156-168 (*supra* footnote 335).

[350] See an analysis of the provision which established such a regime (Article 20 Act 287/90) in GHEZZI, F. and MARCHETTI, P. (1993): "I rapporti dell'Autorità garante della concorrenza e del mercato con le autorità di vigilanza settoriale", in *Concorrenza e Mercato*, p. 205.

[351] See FATTORI, P. (1998): "Brevi notte sulla ripartizione di competenze fra Autorità Garante della Concorrenza e del Mercato e Autoritá per le Garanzie nelle Communicazioni", in *Concorrenza e Mercato*, no. 6, pp. 483-497.

6.3. DUAL STRUCTURES.

6.3.1. General.

126. General. Both in the US[352] and in the Member States of the European Union a common tendency to provide an institutional reflect to the duality of mechanisms of intervention has imposed itself. Competition authorities usually have kept the competence to apply the rules on competition in the de-monopolised sectors, included the telecommunications sector. At the same time, sector specific regulatory authorities have been maintained (in the case of the US) or created (EU) for the regulation of the liberalised markets.

This structure allows a clear differentiation between competition Law and the regulatory mechanisms of intervention. Such a differentiation avoids the risk of denaturalisation of both kinds of instruments. On the one hand, the enforcement of the rules on competition is not de-naturalised by the influence of more interventionist mechanisms closely related to sector specific objectives. On the other hand, regulatory mechanisms (with a very limited tradition in most of the European States) have a better chance to be fully implemented if they are the only ones at the disposal of the regulatory institution.

Besides, the institutional differentiation in relation to the instruments of intervention allows the introduction or development of beneficial relationships

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[352] The American institutional structure is characterised by its complexity. Antitrust authorities coexist with the powerful Federal Communication Commission (FCC), the most traditional sector specific regulator in the world. The American experience cannot be considered an inspiring model, as the dual jurisdiction for the consideration of the behaviour of the undertakings in the telecommunications markets introduces an excessive burden on them, at the same time that increases legal uncertainty, as the standards for the consideration of the operation by the FCC is not only different from the antitrust authorities (see US v. FCC, 652 F.2d D.C. Cir 1980), but also rather vague. See RILL, J. (2000): "Institutional Responsibilities Affecting Competition in the telecommunications Industry", in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gossling Ed., Hart, pp. 667-691; WEISS, J. and STEM, M. (1998): "Serving Two Masters: The Dual Jurisdiction of the FCC and the Justice Department Over Telecommunications Transaction", in *Common Law Conspectus*, vol. 6, p. 195.

between both the instruments of intervention and the institutions implementing them. Firstly, competition between institutions for the development of more efficient solutions to conflicts can arise.[353] The tendency of every institution to increase its influence can be guided, if forced to compete with another institution for the solution of problems and conflicts, to improve its functioning through the development of more efficient procedures (both in effectiveness and in terms of time). Secondly, the dual structure of the institutional framework counter-balances their intervention. In such a way, possible risks related to public intervention by an institution, due "regulatory capture", misuse of power or simply mistakes, can be overcome.

At the same time, the dual structure entails some risks. The most obvious one is the lack of co-ordination between both authorities. Authorities implement different solutions for a single conflict or, even worse, adopt different over-all strategies. Besides, competition between authorities might lead undertakings to try to obtain illegitimate benefits from forum shopping. Lastly, counter-balances between the institutions can delay and even obstruct procedures if they are not well designed.

The balance between the positive and the negative effects of dual structures is determined by the constructive or destructive relation who emerges between them. It can be advanced that a healthy coexistence requires a strong political leadership by the political authorities which the over-all framework, in such a way that both institutions have a clear and compatible view of their objectives and the strategies to reach them. At the same time, a very clear distribution of competencies between the institutions is also necessary, in order not to concentrate the competition on the obtention of competencies, but on the best use of such competencies.

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[353] See McCAHERY, BRATTON, PICCIOTTO & SCOTT (1996): "*International Regulatory Competition and Coordination*", Claredon Press, Oxford.

Important differences can be identified, though, among the institutional solutions implemented in the different States. Some States define very little mechanisms of formal interaction between both authorities, in such a way that the co-ordination between their strategies takes place through informal co-operation or simple formal mechanisms of co-operation between the NCA and the NRA in order to facilitate the co-ordinated character of the public intervention in the sector. Other States have developed a more complex structure in order to ensure such co-ordination and, furthermore, some kind of counter-balance between them.

6.3.2. Parallel Structures.

127. General. The most common position among the Member States of the European Union has been the implementation of a dual institutional structure in which each institution has its own competencies but not formal power to counter-balance the intervention of the other authority. The mechanisms of formal co-operation between the authorities vary among the different States. In any case, the existing formal mechanisms tend to establish mere channels of vague co-operation and not to determine the action of the other authority.

Such a solution not only despises the potential benefits of a more articulated relation between both institutions, but it is also prone to conflict. In some Member States, the lack of a clear political leadership in favour of liberalisation at the highest political levels is allowing NRAs to develop policies that diverge from the more orthodox pro-competitive intervention of the NCAs. At the same time, in some Member States unclear distributions of competencies between both authorities can be identified. As a result, the unavoidable conflicts between the institution are not of a creative character (foster efficiency in the solution of problems) but of a destructive character, as both institutions try to expand their competencies to the detriment of the other.

Furthermore, efficient formal co-operation mechanisms are lacking in many Member States. As a result, forum shopping is favoured, a discrepancy in specific issues is probable, and the already mentioned tendency to divergence in policies is facilitated.

128. The Spanish case. A very clear example of these circumstances can be found in Spain. Firstly, very little tradition of pro-competition policy exists in a State historically characterised by its interventionist tendencies. The regulatory competencies are divided between a Ministry with a strong interventionist tradition, and a powerful independent authority that is considered to be more pro-competition, even if its strategy to promote competition is characterised by its interventionist approach.[354] At the same time, the distribution of competencies between the NCA (*Servicio de la Competencia* and *Tribunal de la Competencia*), and the NRA (*Comisión del Mercado de las Telecomunicaciones*[355]) is prone to conflict particularly over the application of the national rules on competition. Lastly, formal mechanisms of co-operation between both authorities are limited to the application of national competition Law, but for the rest are non existent.

The relation between the NCA and the NRA is of a destructive nature. Very little co-operation exists between the institutions, as little formal mechanisms exist, and informal collaboration is complicated by the existing conflict for competencies. The lack of co-operation strengthens the tendency for their policies to diverge. While the NCA develops an orthodox antitrust policy in the sector, the NRA is more ambitious and is developing an interventionist strategy in order to benefit certain operators against others, not

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[354] See MONTERO PASCUAL, J. J. (1999): "¿Salvaguardia de la competencia o de los competidores? Otra visión de la política española de telecomunicaciones", in *Revista de Derecho de las Telecomunicaciones e Industrias en Red*, vol 5, pp. 145-162.

[355] For an analysis of the Spanish NRA see MONTERO PASCUAL, J. J. (1998): "Naturaleza, estructura y funciones de la Comisión del Mercado de las Telecomunicaciones", in *Revista General del Derecho*, pp. 12305-12318.

only against the operator with significant market power, but also against the new comers which do not invest significantly in the installation of infrastructures.

The most important conflict, nevertheless, is centred on the dispute over the competencies for the application of the national rules on competition (as it seems clear that the NCA have the monopoly over the national application of the Community rules on competition).[356]

The Seventh Additional Provision of the Spanish General Telecommunications Act is clear when it states that the exercise of its powers by the CMT will in any case be respectful for the competencies enjoyed by the national competition authorities. Nevertheless, it follows that this has to be understood within the framework of the functions granted to the CMT by Article 1.Two.2.f of the Liberalisation of Telecommunications Act of 1997. Such provision allows the CMT to adopt general measures for the protection of competition in the markets regulated by the NRA. With regard to concentrations, Article 17.2 LGT is more clear, for it states that the CMT will necessarily provide its non-biding position on any concentrative measure which is to be referred to the Government for its approval.

It thus seems clear that the Spanish regulatory authority is not competent to enforce the national rules on competition, even though it has a small role in the procedure for its application by the national competition authorities. Nevertheless, the CMT is making a very broad interpretation of its power to protect the competitive nature of the telecommunications market and is issuing decisions which develop a reasoning very similar to the decisions applying competition Law, with quotations from the practice of the European Court of

[356] See MARTÍNEZ LAGE, S. (1998): "La Comisión del Mercado de las Telecomunicaciones y el Derecho de la Competencia", in *Gaceta Jurídica de la C.E. y de la Competencia*, no. 136, pp. 1-4, and no. 137, pp. 1-4.

Justice and the European Commission in the application of the Community rules on competition. It has even stated that it is competent to study the potential anticompetitive effects of particular behaviours. It would seem that the CMT considers itself competent to apply the rules on competition, or at least, that it pretends to develop a very similar intervention based on its own competencies.

129. The French case. The French legislation creates more formal mechanisms of co-operation between the NCA (*Conseil de la Concurrence*) and the NRA (*Autorité de Regulations des Telecommunications*).[357] These mechanisms respect the parallel character of the their intervention in the telecommunications markets, but facilitates the co-ordination of such parallel interventions.

Firstly, the NCA is bound to allow the NRA to communicate its non-binding position before adopting any decision on a competition matter regarding telecommunications markets. Secondly, the NRA can formally require the position of the NCA on any point regarding the effects on competition of any measure or action. At the same time the NRA must seek the opinion of the NCA for the definition of the list of operators with significant market power, even if the opinion of the NCA is not binding.[358] Thirdly, the NRA, when acting as a conciliator, must inform the NCA. If a referral to the NCA on the same issue is pending, the NCA can stay its investigation until the end of the conciliation procedures, while the NRA must make a referral to the NCA if conciliation fails. Finally, the NRA must refer to the NCA any

[357] See JENNY, F. (2000): "Safeguarding Conditions for Fair and Efficient Competition in Complex Network Markets: Institutional Issues", in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gosling Ed., Hart, pp. 624-628.

[358] The German legislation requires the approval by the NCA of the list prepared by the NRA, see WOLF, D. (2000): "Institutional Issues of telecoms Regulation: Discussion Points", in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gosling Ed., Hart, pp. 741-748.

potential anticompetitive practice, and can even require the NCA to make its decision within a thirty days term.

It seems that the clear distribution of competencies has avoided conflicts such as the ones that emerged at an early stage in Spain. Both authorities respect each other's position and have formally consulted each other even if it was not required by Law. The divergence of the policies of both institutions is obstructed by the fact that the decision of both authorities are subject to judicial review in front of the same body: the Court of Appeals of Paris. Nevertheless no real competition between the institutions seems to emerge from this framework.

6.3.3. Counter-Balanced Structures.

130. General. The co-existence of a competition authority and a regulatory authority can be structured in such a way as to provide a counter-balance not only between both institutions but also between both instruments of intervention.

The introduction of formal mechanisms for counter-balancing the actions of the institution can have positive effects. Firstly, "regulatory capture" is obstructed, as market players have to capture more than one institution, which is always more difficult. Besides, granting powers to the competition authorities to counter-balance the actions of the regulatory authorities obstructs capture since a non-specialised institution is more difficult to be captured than a sector specific institution. Secondly, such counter-balance tends to ensure a better co-ordination of the intervention of both kinds of institutions, as an overall agreement between them is necessary for the development of their activity, as one institution can block the actions of the other. Third, such mechanisms can directly enhance the efficiency of public intervention. The assignation of the role of arbitrator to one of the institutions in a case of conflict between the other institution and a regulated company allows a simple

and time-efficient resolution of the conflict by an institution that is close to the sector and understands its problems. In such a way, the authoritarian tendency of the public institutions is obstructed, and judicial review -time-consuming and risky- is not encouraged.

Counter-balancing mechanisms can have beneficial effects not only from an institutional perspective, but also from the perspective of the instruments of intervention used by the different institutions. The risk of over-regulation and the risk of de-naturalisation of competition Law can be minimised if each kind of intervention is counter-balanced by a review from the institution competent for the application of the other instrument of public intervention.

Counter-balanced models can have, at the same time, negative effects. The most important one is the tendency to complicate the administrative procedures with endless administrative reviews, which in any case can be subject to a final judicial review. There is then the risk of making administrative procedures complicated, time-consuming and cumbersome for the industry. In order to avoid such a risk, political leadership and a precise distribution of competencies are, once more, necessary. At the same time, a sound design of the counter-balancing mechanisms is required, in order to allow for the solution of institutional conflicts and avoid mutual blockage. In this sense, pre-eminence might be granted to one of the institutions, and a common, specialised and time-efficient judicial institution for appeal can ensure solutions for situations of blockage.

131. "Sun-set clauses". The most radical example of counter-balancing mechanisms is the power granted in certain Member States to specific bodies to determine the end of the transitory period from monopoly to effective competition and, therefore, the validity of the asymmetric regulatory mechanisms bestowed on the regulatory authorities. Such powers are usually denominated "sunset clauses".

In Germany, for instance, an independent body of experts, the Monopolies Commission, asses the conditions of competition in the telecommunications market at regular intervals and issues recommendations as to whether sector-specific regulation is still necessary.[359] In the Netherlands, a clause was introduced according to which four years after the implementation of the new regulatory framework, it will be assessed whether transitional regulation is still necessary.

132. The British case. The UK was the first Member State to abolish the exclusive right enjoyed by the public authorities for the provision of telecommunications services, the first Member States to fully privatise the incumbent operator, and the first Member State to establish a regulatory authority, the Office of Telecommunications (OFTEL).[360] At the same time, competition Law has not been particularly strict, and only the adoption of the 1998 Competition Act has created a regime assimilable to the existing regimes in the other Member States.

The British institutional scheme has been characterised by its complexity, with a number of institutions empowered to intervene in the telecommunications markets, including OFTEL, the Secretary of State, the Director General for Fair Trading and the Monopolies and Mergers Commission. Counter-balancing mechanisms have always existed. Amongst them, the regime for the modification of licence conditions, and the concurrent applications of Competition Law are particularly interesting.

The centres of the British regime on telecommunications are the licences granted to the operators. Following the Common Law tradition, and as a result of the lack of pressure from Community Directives, as the sector was already de-monopolised in the UK, very few general provisions rule the provision of

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[359] *Vide* WOLF (2000) (*supra* footnote 358).

telecommunications services in the UK. It is for the licences (individual, general or class licences) to define the conditions for the provision of such services.[361] As a result, the granting of the licences, and therefore the definition of the conditions contained in the licences, and the modification of such conditions after the granting of the licence are the most important regulatory mechanisms in the UK.

Licences are granted by the Secretary of State after consultation with the Director General of OFTEL. As a result, it is the Government the body which directly defines the policy through the adoption of the conditions included in the licences, even if the regulatory independent agency has the prerogative to be consulted. With regard to modifications, initially, it could be sustained that modifications resulting in a radical transformation of the licence should be implemented through the adoption of a new individual licence by the Secretary of State, as it is the body that defined policies. On the contrary, modifications which merely adapt the existing policies to new circumstances (even if the borderline between these and the last modifications is difficult to define) do not require the intervention of the Secretary of State. Two different procedures were established by the 1984 telecommunications Act.

On the one hand, the modification can be agreed by OFTEL's Director General with the holder of the individual licence, following the procedure defined in section 12 of the 1984 Act. OFTEL's Director General can make a proposal to the licensee. The Secretary of State has the power to force the Director General to withdraw the proposal of modification. If it is not the case, and the licensee accepts the modification, it is introduced. On the other hand, in case the modification proposed by the Director General is not accepted by the

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[360] See LONG, C. (1995): "*Telecommunications Law and Practice*", Sweet & Maxwell.

[361] Most of the Member States have granted a central role to the licences for the definition of the conditions ruling the provision of services, but the UK experience is unique, as very few general provisions exist even as regards the ruling of the granting of the licences themselves.

licensee, he might make a referral for the Monopolies and Merger Commission (MMC), in order for it to study the effects on the public interest. With the approval of the MMC, the Director General can then modify the licence.[362]

Such a process is extremely interesting, as it fosters a non-authoritarian intervention by the Director General, the time-efficient arbitration of an administrative body (6 months), and the control of the regulatory intervention by a competition authority, which studies the modification from a pro-competition perspective. At the same time, the political leadership of the political authorities is ensured by the possibility of the Secretary of State to adopt a new licence, as well as by his power to withdraw the proposals of modification from the Director General.

With regard to the application of the national rules on competition,[363] it is interesting to note that the British regulatory authorities are the only ones in the EU to clearly enjoy the competencies to apply such rules, even if concurrently, with the competition authorities. The 1998 Competition Act has introduced new mechanisms of co-ordination for such concurrent application.

As it is described in the Guidelines issued by the Office of Fair Trading and all the sector specific regulators, including OFTEL,[364] with a few exceptions[365] the Director General of OFTEL has all the powers of the Director General of Fair Trading to apply and enforce the 1998 Competition Act to deal with anti-competitive agreements or abuse of market dominance relating to the telecommunications markets. Furthermore, it has been agreed that in general, it

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[362] *Vide* LONG, pp. 54-56 (*supra* footnote 360).

[363] Substantive as well as procedural issues are studied in the Draft Guidelines on the application of the Competition Act in the telecommunications Sector published in January 1999 by OFTEL and the Office of Fair Trading. See also LANDAU, J. (1997): "Fair Trading in Telecommunications", in *European Competition Law Review*, no. 7, pp. 446-450.

[364] Office of Fair Trading (1998): "*Concurrent Application to Regulated Industries*", London.

will be for the regulator to handle the investigation, adopt a decision and enforce it.[366] The Director of Fair Trading is, in any case, consulted by the regulator in all the cases, and receives a copy of all the notifications for guidance, the notifications of agreements or conduct for clearance and complaint.

The Director General of Fair Trading might require dealing with a case if it is better placed to do so. Different factors have been agreed in order to determine who is better placed to deal with a case. Among those factors, the previous contacts with the parties or complainants, and the recent experience as regards the issue are appreciated. In 1997 the Concurrency Working Party was created for the resolution of the conflicts regarding concurrency. This body is formed by a representative of the seven regulatory bodies existent at that moment in the UK (among them OFTEL) and is chaired by a representative of the Office of Fair Trading. The Concurrency Working Party defines general principles in relation to concurrency and is the forum of the exchange of information about the cases being handled by each authority. At the same time, it is the body which decides which authority is better suited for handling a case if the Director General of Fair Trading and the Director General of one of the regulatory authorities do not reach an agreement about it.

The British legislation contains other provisions in order to increase the transparency and effectivity of such a framework. Firstly, the 1984 Act has been amended so as to establish that in those cases in which the Director General applies the rules on competition, he will not make use of his regulatory powers. Secondly, it has been agreed that the licence conditions which imposed

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[365] Such exceptions are mostly related to the definition of procedures and the issue of guidance on penalties, even if in such occasion, the Director General of fair Trading has to consult with the regulators.

[366] The Advisory Body on Fair Trading in Telecommunications was created in December 1996 in order to advise OFTEL's Director general on the enforcement of the Fair Trading condition included in all the individual licences.

the obligations not to engage in anticompetitive practices will be eliminated. Third, the amended 1984 Act foresees that in a case where it is considered that it is more appropriated to proceed under the 1998 Competition Act, he will not take licence enforcement action. Finally, common appeal bodies, both for administrative and for judicial review are established.

As a conclusion, the British system fosters the application of the rules on competition over the sector specific rules contained in the licences, but at the same time, the application of the rules on competition is bestowed rather in the regulatory authorities than in the competition authorities. Flexible mechanisms have been informally introduced in order to ensure the resolution of conflicts derived from the concurrent competence for the application of the rules on competition. All these mechanisms tend to ensure the distinction between regulatory and antitrust intervention.

133. Counter-balancing intervention of the EC authorities. It cannot be forgotten that the Member States' measures of intervention in the telecommunications markets are subject to the scrutiny of the European Community authorities. As stated by the Commission "[a]t Community level, it is also important to ensure that Member States do not implement different patterns of regulation which lead to market variation, increasing cost to end-users and a fragmentation of the single market."[367]

European authorities enjoy various mechanisms to control and balance the intervention of the national authorities in the telecommunications markets.[368]

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[367] COM(2000) 395, Proposal for a Directive of the European Parliament and of the Council on access to, and interconnection of, electronic communications networks and associated facilities, 12.7.2000, Brussels.

[368] For an extremely interesting analysis of the relation between the NRAs and the European Commission, see TEMPLE LANG (1998): "Community Antitrust and National Regulatory Procedures", in "*Fordham Corporate Law Institute*" pp. 297-334.

The European Commission can initiate infringement procedures against Member States following the procedure defined in Article 169 EC Treaty, in case Member States do not implement the relevant directives, or do not implement them completely or faithfully. It is an open debate whether Community harmonising Directives are exhaustive or not, but it can at least be claimed that Member States cannot expand the obligations on the operators established in the Directives (mostly in the 97/33/EC Directive) as such behaviour might amount to a barrier to market access to new entrants. Article 169 EC Treaty might become an instrument against over-regulation by the Member States.[369]

At the same time, it is possible for the European Commission to intervene against the Member States for the breachment of the rules of the Treaty, and particularly the rules on competition, with regard to their relation with their public undertakings, the undertakings with special or exclusive rights and the undertakings vested with the management of a service of general economic interest, as established in Article 86 (former 90) EC Treaty. With regard to the immediate protection of the general interest, national measures must not restrict competition any more than is necessary to achieve a legitimate purpose in the general interest.[370]

Moreover, the Community authorities can intervene in case of breachment by the Member States of the *effet outil* of the EC Treaty rules on competition. Even if Articles 81 and 82 EC Treaty apply only to undertakings, the obligation for Member States to ensure the application of the rules contained in the Treaty (defined in Article 5) have been interpreted as to force Member States not to

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[369] *Vide infra* Chapter 10.3.2. Antitrust Counter-Balances Regulation.

[370] See BLUM, F. and LOGUE, A. (1998): "*State Monopolies under EC Law*", John Wiley & Sons, Chichester.

impose or favour anticompetitive practices.[371] For instance, NRAs must not authorise or approve any behaviour that breaches the treaty. Therefore, the European authorities can obstruct the implementation by the NRAs of measures that constitute a clear breach of Articles 81 or 82 EC Treaty.

134. New mechanisms of control. The reform of the legislative framework proposed by the Commission as a result of the 99 Review strengthens the role of the European Commission.

The Commission proposal introduces a great deal of flexibility in the regulatory framework. As competition emerges at different rhythms in the more traditional telecommunications product markets (fixed telephony infrastructures and services), and as new bottlenecks in different segments appear (mobile telephony, set-top boxes etc.) a more flexible framework was required.

The Commission proposed a framework that would depart from the definition at a centralised level of the market segments to be scrutinised by NRAs in order to be regulated. The Commission would produce an annual list of segments. NRAs would only be in the position to analyse other markets with the explicit permission from the Commission.

In case an NRA would find market distortions in one of the segments in the annual list published by the Commission, it could impose regulatory obligations, but only those included in a closed list in the directive. A specific permission from the Commission is to be obtained by an NRA in order to introduce a different regulatory obligation.[372]

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[371] See VICIANO PASTOR, J. (1995): *"Libre competencia e intervención pública en la economía. Acuerdos restrictivos de la competencia de origen legal"*, Tirant lo Blanch, Valencia.

[372] See COM(2000) 393, Proposal for a Directive of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services, 12.7.2000, Brussels; and COM(2000) 395 Proposal for a Directive of the European Parliament and of the Council

Therefore, Community institutions can play an important counter-balancing role, as they can limit the over-regulation of the national regulatory authorities with different mechanisms, most of them related to their role as competition watchdogs, but also of a regulatory nature if the proposal of the Commission is successful.

6.4. CONCLUSIONS.

135. Institutional frameworks. Despite the proposals to concentrate the competencies for the application of competition Law and sector specific regulation in a single institution, Member States have mostly opted to maintain the competence of the NCAs for the application of the rules on competition to the telecommunications undertakings, and to create sector specific regulators for the application of the sector specific regulation.

Two kinds of relations between the NCAs and the NRAs can be distinguished. On the one hand, both kinds of institutions can intervene in parallel according to their competencies, without a direct interaction between them. Different degrees of co-operation between the authorities can be found in this kind of relation. In some cases, only informal co-operation exists. In other cases, some formal channels of co-operation for the co-ordination of policies or the exchange of information have been established. Finally, some examples of a tighter formal co-operation can be found, with the intervention of the other authority for the adoption of certain decisions. In all these cases, each institution behaves largely independently from the other, as no effective limitations are imposed on them by the other institution.

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on access to, and interconnection of, electronic communications networks and associated facilities, 12.7.2000, Brussels.

On the other hand, a more complex relation can be established through formal mechanisms of counter-balance of the actions of both kinds of institutions. According to this model, the action of one institution depends, to a certain extent, on the previous action of the other, or on the co-ordinated intervention between them. Indeed, in some cases, one of the institutions is competent to review the actions of the other one.

136. Evaluation. The existence of a different set of institutions for the application of competition Law and for the regulation of the liberalised markets can have beneficial effects, at least during the period of transition from monopolies to effective competition. Such a separation stresses the different nature of both kinds of intervention, what allows the full development of both of them (particularly in those States with little tradition of indirect intervention) and obstructs the denaturalisation of each instrument (particularly of the rules on competition).

Institutional differentiation can have other beneficial effects. It can promote competition between administrations for the efficient solution of the problems and conflicts between the operators. At the same time each institution can counter-balance the excesses of the other, excesses derived from mistakes, regulatory capture, or phenomena as over-regulation or the application of the rules on competition for the solution of conflict out-side of their scope.

In any case, certain requirements have to be met for the obtention of such benefits. Firstly, a clear liberalising strategy established by the Legislator and the highest political authorities is necessary in order to avoid divergences in the strategy of the different institutions. Secondly, a clear-cut distribution of competencies is necessary in order to avoid destructive conflicts between institutions for the mere obtention of new powers. Third, formal mechanisms of collaboration enhance co-ordination of policies and actions. Finally, formal

mechanisms of interaction have to be balanced and provide solutions for institutional conflicts so that no blockage exists.

If these requirements are not met, there is a high risk of conflict between the NCAs and the NRAs. Firstly, divergent policies could arise. Secondly, lack of co-ordination in specific cases could produce legal uncertainty in the sector. Third, competition between institutions could become destructive, as only centred in the obtention of new competencies, promoting forum shopping from the operators. Finally, the complexity of the institutional framework could produce time-consuming administrative procedures, situations of blockage of institutional conflicts and un-necessary intervention of the judicial authorities.

In any case, as the period of transition reaches its end, the institutional framework should be reconsidered. It is widely shared that independent regulators will have a very technical and reduced role once competition arises and the asymmetric regulation disappears, while competition authorities will take the lead on the public intervention in such markets. As a result, concentration of activities in the NCAs, following the Australian example could be considered. Otherwise, formal mechanisms ensuring the pre-eminence of the NCAs could be granted, in order to maintain a mere technical role for the regulatory authorities.

The co-existence of competition and regulatory authorities both at a national and at a Community level could also have another interesting beneficial effect in relation to the end of the transitional period. Competition authorities could be bestowed with the power to determine the end of the transitional period, as such authorities have the tools to certify the existence of effective competition. Nevertheless, it has to be taken into account that such authorities would benefit from the elimination of the transitional sector specific regulation, as it would mean the attainment of the central role in public

intervention in the market. It is for these reasons that a more balanced solution is necessary.

PART III

NETWORK ACCESS

CHAPTER 7

NETWORK ACCESS: NOTION AND RELEVANCE

SUMMARY: 7.1. The notion of network access. 7.2. The relevance of network access. 7.3. Conclusions.

7.1. THE NOTION OF NETWORK ACCESS.

137. Introduction. Public intervention on network access acquired a central role in the European telecommunications arena when value-added services were de-monopolised.[373] No competitive constraint existed on the operators enjoying the legal monopoly over the telecommunications infrastructures to provide access to their networks to the new service providers or final users. The lack even of potential competition in the legally monopolised infrastructure markets excluded the definition of access

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[373] *Vide supra* Chapter 3.4.3. Liberalisation of the Telecoms Markets (1987-1999).

conditions by supply and demand mechanisms. Public intervention mechanisms to ensure network access at fair conditions were developed in order to ensure that refusals to grant access to monopolised infrastructures would not exclude new comers from the services markets.

Full liberalisation of the European telecommunications markets eliminated all the legal barriers to competition, but technical and mostly economic barriers still allowed the incumbents to abuse the power derived from the control over the only existing universal telecommunications network in each Member State. Public intervention devoted to ensure network access at fair conditions has been perceived as necessary in order to accelerate the process of reform of the markets while ensuring the protection of the general interest.

Intervention on network access is supposed to allow the development of alternative networks, to obstruct exclusionary practices in the services markets and to guarantee the universal availability of telecommunications services. Nevertheless, it has also been perceived that imposing compulsory access as well as access conditions entails risks. The emergence of competition can not only not be accelerated but indeed prevented if the incentives for the development of alternative infrastructures are significantly reduced and competition is distorted. It is widely agreed that the "need to strike a balance so as to encourage efficient investment in alternative infrastructure and enable the development of service competition at the retail level".[374]

Mechanisms derived from the application of the rules on competition (essential facilities doctrine) and of a regulatory character (Open Network Provision framework) have been developed in order to obstruct the negative effects of refusal to grant access. Nevertheless, competition Law, on the one

[374] LEWIN and ROGERSON (1999): "*A Review of the Interconnect Directive. Initial Proposals for Discussion*", European Commission, Brussels, p. 15.

hand, shows important limitations with regard to the imposition of compulsory access and furthermore the definition of access conditions. Sector specific regulation, on the other, risks introducing obstacles to competition. However, a balanced approach with the continuous interrelation between regulation and competition Law might ensure an efficient intervention for the emergence of effective competition. Sector specific regulation can complement the rules on competition in order to develop a more aggressive strategy, while the rules on competition can limit the risks of over-regulation.

138. The notion of network access. No definition of the notion of network access can be found in the community directives. However, it could be broadly defined as the use of the facilities that conform a network by an entity different from the owner.[375]

The new legislative framework proposed by the Commission as a result of the 99 Review contains a definition of network access along such line: "Access means the making available of facilities and/or services, to another undertaking, under defined conditions, on either an exclusive or non-exclusive basis, for the purpose of providing electronic communications services. It covers, *inter alia*: access to network elements and associated facilities and services, [...] access to physical infrastructures [...] access to software systems [...]. Interconnection is a specific king of access implemented between public network operators [...]."[376]

Community directives have developed a special regime for interconnection, where access adopts the form of the connection between two networks, or as it is defined by the directives, interconnection is the "physical

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[375] COM(1999) 539, The 1999 Communications Review , of 10 November 1999, in page 25 states that "access is a generic concept covering all forms of access to publicly available network and services, whereas interconnection refers to the physical and logical linking of networks".

and logical linking of telecommunications networks used by the same or a different organisation in order to allow the users of one organisation to communicate with users of the same or another organisation or to access services provided by another organisation".[377]

139. Categories. From an abstract point of view, it is possible to differentiate three different kinds of access: access for mere interoperability, access to market presence, and access by final users.

Firstly, access can be required merely to ensure interoperability between different operators. Even if an operator disposes of a fully operative telecommunications network which allows a client to communicate with other clients and satisfy in this way the most basic demands, it is clear that such clients will only be able to communicate with users contracting with another operator if both operators connect their facilities. This is the case, for instance, of international interconnection, or peering agreements between ISPs.

In an equilibrated market, most operators would be interested in connecting their networks in order to provide universal connectivity for the benefit of their clients.

Secondly, access can be required to complement the facilities at the disposal of a particular operator in order to be able to commercialise its service. This is the case of a service provider with no infrastructures, or the case of a new comer that disposes of a backbone network, but needs access to the local loop which serves its clients. Special access, as defined in the directives, fits under this category, as well as some kind of "asymmetric" interconnection.

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[376] Com(2000) 384, Proposal for a Directive of the European Parliament and of the Council on access to, and interconnection of, electronic communications networks and associated facilities, Article 2, 12.07.2000, Brussels.

[377] Article 2(7) of Directive 90/387/EEC as amended by Directive 97/51/EC.

Operators in control of wide networks might not have the incentives to provide such access, as it might allow new comers to provide services while developing alternative infrastructures which in the future will compete, or provide services in competition with those of the operator providing the facility.

Finally, access can be required by final users in order to benefit from a connection that allows them to receive the different telecommunications services. It is the very same essence of competition in the market for operators to try to maximise their profits by providing their services to a significant share of potential clients. Nevertheless, it might be the case that some clients might not be profitable for the operators. Providing access to clients in scarcely populated areas can be too expensive, and at the same time, some clients might not have the necessary income to pay the reasonable prices offered by the operators.

7.2. THE RELEVANCE OF NETWORK ACCESS.

7.2.1. Promotion of Competition.

140. De-monopolisation and access. Two well-known characteristics of the network industries, the economies of scale and the network externality, introduce significant barriers to entry to the de-monopolised telecommunications markets. The sector presents major economies of scale, as it is widely accepted that the unit costs faced by a new entrant are higher for the provision of capacity in the long distance segment and particularly exorbitant in the local loop.[378] Besides, as a result of the some how obvious network

[378] Some data suggest that the unit cost might be even eight times bigger for an access provider in suburban areas with a market share bellow 10% than for an access provider in the same area with a market share of 100%, see LEWIN, David and MATHEWS, John (1998): "Access networks and Regulatory Meassures", OVUM for DG XIII, European Commission, Luxembourg, pp. 23-25.

externality effect, a network increases its value exponentially as it increases its reach.[379] Furthermore, the exclusive rights enjoyed for decades by national monopolies have allowed them to develop infrastructures that conform the only universal telecommunications network in each country. The former monopolies, therefore, benefit from all the existing economies of scale as well as from the network externality effect.

The barriers derived from the network character of the telecommunications industry and the traditional exclusive rights become particularly important if combined with sunk costs which reduce entry as well as exit freedom. Predominance of sunk costs imposes a further burden on new comers, at the same time that it creates scope for strategic behaviour by the former monopolies.[380] As a consequence, effective competition and even potential competition might be excluded from some telecommunications markets.

Sunk costs are not predominant in telecommunications services markets, nor are economies of scale so decisive. What reduces barriers to new comers in such a way that effective competition can emerge without major obstacles in such markets. Sunk costs have a relevant weight in telecommunications infrastructures markets, and therefore such markets might have a stronger tendency to monopolisation. However, it has to be taken into account that economies of scale might become exhausted, so they do not necessarily reach the whole market. This seems the case of long-distance telecommunications infrastructures which, despite of their sunk costs, are open to competition. As regards local infrastructures, technological progress is creating alternative

[379] A network with only one point of contact has a value of zero, and reaches its maximum value when all the potential parties are connected to it.

[380] KNIEPS, Günter (1999): "Access to networks and interconnection: A disaggregated approach", in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gossling Ed., Hart, p. 152.

infrastructures that significantly reduce the costs of developing comprehensive networks. Therefore, real bottlenecks in the telecommunications industries seem exceptional, even if they certainly exist particularly in some elements of local loop infrastructures. It has been pointed that it is not simple to clearly identify the limits of effective and sustainable infrastructure competition, and that it would be wrong for regulator to attempt to fix such limits without flexibility.[381]

Competition might reach most of the telecommunications markets, but it is clear that time is necessary for the emergence of effective competition, particularly in those markets which require the installation of comprehensive infrastructures. As a result, effective competition did not appear instantaneously after de-monopolisation in markets without decisive barriers to entry.

The control by the former monopolists over bottlenecks not only provides a monopolistic position in such markets. Moreover, such market power could be used by the incumbents to strengthen their dominance in neighbouring markets in which the bottleneck is essential. This is the case, firstly, of the general market of telecommunications infrastructures, as new comers with their own infrastructures need to interconnect them to the incumbent's infrastructures, and in particular to the bottleneck elements. Secondly, new comers to the services markets need to reach their potential users through installed infrastructures. They might decide to install them themselves, but it is obvious that it is not viable for each one of the hundreds of service providers to install their own network. It is therefore necessary for them to contract the provision of access to users with an operator that exploits existing infrastructures. The control over a bottleneck, in such a situation, grants market

[381] *Vide* LEWIN and ROGERSON (1999) p. 16 (*supra* footnote 374).

power also in the downstream service market for which the bottleneck is essential.

Furthermore, even if the segments in which there is very limited scope for competition are exceptional, it seems clear that they will survive the liberalisation process. As a consequence, some kind of public intervention, subsidiary, limited and compatible with competition, should also survive the transitory period from monopolies to effective competition, in order to govern the nowadays unavoidable market failure.

141. Oligopolies and access. As the process of transition from monopolies to effective competition evolves, and as new electronic communications networks and services appear, the focus of the debate on access is changing.

The monopolistic position of the incumbents is being challenged in most product markets all over Europe. For instance, a significant amount of European backbone networks are being deployed and already offer services in Europe. Competition is also emerging, albeit at a much slower pace, in the local loop, through the installation of cable networks and wireless local loop networks all over Europe.

In any case, it seems clear that only major routes (for instance London-Paris-Frankfurt) might attract an important number of network operators. Most of the routes, as well as the local loop, will only attract a reduced number of operators. Concentration, as well as other relevant features of the telecommunications markets such as the relevance of sunk costs and the lower variable costs, lead to a oligopolistic market structure.

At the same time, new electronic communications networks such as mobile telephony networks or digital television networks (whether satellite, terrestrial or cable networks) due to the economies of scale and scope, the network externality effect, the relevance of sunk costs and other reasons, have

also proven to have a strong tendency to oligopoly. Particularly relevant is the case of networks based on the use of radioelectric frequencies. The scarcity of such a resource lead unavoidably to the concentration of the market, as the number of players is necessarily limited due to physical limitations.

Both tendencies are shifting the focus of the debate from the issue of access to the incumbents' networks, to the issue of access to oligopolistic networks.

142. The relevance of network access. Access to the telecommunications networks at determined conditions can eliminate or at least reduce the barriers to entry derived from the network externality as well as from the economies of scale of the network.

Access allows, first of all, the network externality effect to be overcome, as it allows all users to intercommunicate despite contracting with different providers.[382] Secondly, access to the incumbent's networks at prices oriented to costs would allow for the distribution of the benefits of economies of scale among all the market participants. This would mean the elimination of another barrier in the infrastructures markets. Finally, network access would eliminate the barrier created by the vertical integration of the incumbent. Access to the network in the same conditions for all the service providers, including the incumbent, would eliminate the exclusionary effects derived from the discrimination in its own favour exercise by the incumbent.[383]

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[382] For the effects of lack of interoperability in the early period of US telecommunications history *vide supra* Chapter 2.4.1. Origins and Free Competition in the US Telecom Markets (1876-1921).

[383] See DEBAILLE, REPIQUET, CARTWRIGHT and DUNKLEY (1997): "*Equal Access and Interconnection*", European Commission, Brussels; LEWIN and KITCHEN (1994): "*Interconnect. The Key to Effective competition*", OVUM, London; LONG, VAN LIEDEKERKE and RYAN (1995): "*Competition Aspects of Interconnection Agreements in the Telecommunications Sector*", European Commission, Brussels; WIK (1994): "*Network Interconnection in the Domain of ONP*", European Commission, Brussels.

Network access and its conditions were the centre of the liberalisation debate. Network access played a fundamental role in the strategy aimed at eliminating and reducing the barriers to entry that complicate the emergence of effective competition in the telecommunications sector after de-monopolisation. Public intervention on network access was perceived a necessary for the reduction of the incumbent's market power and the emergence of effective competition in the market.

It is important to point out, though, that public intervention on network access might also be relevant after the period of transition after de-monopolisation. The oligopolistic tendency of most network industries, not only the traditional public telephony, but also new industries such as mobile communications or digital television might also require some kind of public intervention in order to obstruct attempts to monopolise.

7.2.2. Immediate Protection of the General Interest.

143. Universal access. Network access not only benefits new operators, but also final users. Citizens' access to the most basic telecommunications services is increasingly considered as a fundamental instrument for the participation of individuals in economic, social and even political activities,[384] and as a result, public authorities have considered the need to ensure the universal availability of such access, so that every citizen can benefit from it.

Universalisation covers two different issues. Firstly, universal geographic availability, as universalisation would only be possible if access was possible to all users independently of their geographical location. Secondly, access should take place at reasonable conditions. Affordability, in particular is considered relevant in order to guarantee access to the services. Access to networks or

[384] See GRAHAM, CORNFORD and MARVIN (1996): " The Socio-economic Benefits of a Universal Telephone Network. A Demand-side View of Universal Service", in *Telecommunications Policy*, vol. 20, no. 1, pp. 3-10.

services at similar conditions independently of the location is usually connected to this point.

Traditionally, the mere presence of public authorities in the telecommunications sector in the form of the national public monopolies was supposed to ensure the satisfaction of the general interest. Even if the geographic expansion of the telephony network took place usually behind demand,[385] universal coverage was reached in most of the member States, even if only recently in some of them.

No particular effort was devoted to ensure the affordability of the service to the most disfavoured groups as very few specific programs for such groups were implemented. On the contrary, a general policy to provide services of a minimum quality for similar prices in all the territory was undertaken by the national monopolies. Cross-subsidies were frequent not only from urban to rural areas, but also from long-distance to local services and from business users to residential users. Such cross-subsidies undoubtedly improved the affordable character of the services. Nevertheless, it is not clear whether such a strategy was always conscious nor efficient.

On the one hand, it can be argued that some of the cross-subsidies were not the result of a conscious strategy but the mere result of the evolution of the sector. The lack of a sound cost accounting methodology might have made possible the divergence between costs and prices. As long-distance communications costs were reduced, the mere maintenance of the price structure would over the years produce a cross-subsidy from such services to the local services. Political pressure not to raise residential users' bills reinforced such a tendency. On the other hand, such policy was criticised because of its inefficiency. The generalised cross-subsidies introduced major

[385] For an overview of the delays in the development of the French network *vide supra* Chapter 3.4.4. Public Monopolies (1900-1987).

distortions in the sector which benefited some groups without an objective necessity (high income residential users), and imposed an excessive burden on other groups (low-income residential users making use of long-distance communications), without ensuring effectively the universal affordability of the services.

The reform of the European telecommunications markets was intended to increase the satisfaction of the consumers, as competition was expected to increase efficiency and therefore reduce costs and prices for better quality products. In this way, universalitation of the services would be facilitated. Nevertheless, those Member States with a tradition of distrust on the interrelation of private interests as generator of the general interest and a more interventionist approach, required the introduction of mechanisms of public intervention devoted to immediately ensure the satisfaction of the general interest, that is, to ensure the universality of the basic services.

144. Universal access and liberalisation. The process of reform of the European telecommunications markets required the elimination of the traditional mechanism of intervention for the increase of access to the network. Competition excluded internal cross-subsidies due to the well-known phenomenon of screaming.[386] Some actors tried to obstruct the liberalisation process by connecting the elimination of the exclusive right and the elimination of public intervention for the protection of the general interest. Access to the telecommunications networks by citizens became then one of the fundamental issues in the liberalisation debate, and specific mechanisms were required in order to ensure such a general interest objective.[387]

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[386] See OECD (1991): "*Universal Service and Rate Restructuring in Telecommunications*", OECD, Paris.

[387] See Analysis (1997): "*The Future of Universal Service in telecommunications in Europe*", Analysys, Cambridge; GRAHAM, CORNFORD and MARVIN (1996): "The Socio-economic Benefits

It was argued that technological progress had reduced the costs of the provision of the most traditional telecommunications services,[388] and that the maturity of the traditional telecommunications markets had ensured the virtual universalitation of the service.[389] It was pointed that the introduction of competition would foster a further reduction on costs and prices and therefore beneficial effects on the affordability of the service. Nevertheless, the defendants of the traditional mechanism of intervention for the protection of the public interest forced the introduction of mechanisms devoted to ensure the universality of access to the most basic telecommunications services.

7.3. CONCLUSIONS.

145. Final. Public intervention in relation to network access has become the fundamental mechanism of intervention in the liberalised telecommunications markets.

Compulsory access and the definition of compulsory access conditions has been imposed on operators with significant market power in order to promote the emergence of competition, in the transitory period from monopolies to effective competition.

It has to be pointed that as the incumbents' market power diminishes, and as new electronic communications services are introduced, the focus of the debate is shifting from the need to counter-balance the market power of the incumbents, to the need to avoid the anticompetitive effects of oligopolistic

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of a Universal Telephone Network. A Demand-side View of Universal Service", in *Telecommunications Policy*, vol. 20, no. 1, pp. 3-10

[388] See BERNT, KRUSE and LANDSBERGEN (1993): "Impact of Alternative Technologies on Universal Service and Competition in the Local Loop", in *Telematics and Informatics*, vol. 10, no. 4, pp. 359-377.

[389] See Analysys (1997): "*The Future of Universal Service in Telecommunications in Europe*", Analysys, Cambridge, p. 63.

structures both in the more traditional markets such as fixed telephony and in new markets such as mobile communications and digital television.

In parallel, general interest objectives recommend that public authorities guarantee access for all consumers to some electronic communications networks and services.

Two are the main instruments of public intervention at the disposal of the Community and national authorities for imposing network access and the condition of such access. Both of them suffer limitations and entail risks, but they complement each other and can even mutually restrict their most negative tendencies.

On the one hand, refusals to deal were often considered abusive under Article 82 EC Treaty (former 86). The transplantation of the American essential facilities doctrine was supposed to strengthen the European refusals to deal principle. The European Court of Justice, however, does not seem to back an enthusiastic application of Article 82 to refusals to grant network access.

On the other hand, sector specific regulation was adopted by the community directives under the name Open Network Provision. These rules can provide a legal base for a more aggressive intervention, and for this reason entail also the risk of over-regulation.

It has to be noticed at this point that network access entails at the same time dangerous risks. The imposition on the incumbent of the obligation to provide access to his competitors could amount to a confiscation of its assets. This is particularly important if it is taken into account that most Member States have privatised the former monopolist and have received a significant income precisely because investors paid for the control of the public switched network. It would distort the market to impose *ex post* excessive obligations on such shareholders. Furthermore, the excessive facilities granted to the new comers for the access to the incumbent's network could create a new barrier to

entry to such markets, as it would eliminate the incentives for the installation of alternative infrastructures. As a result no effective competition could arise in such markets and the barriers to entry both to the infrastructures and services markets would never disappear.

CHAPTER 8

COMPETITION LAW AND NETWORK ACCESS

SUMMARY: 8.1. Introduction. 8.2. The US origin of the essential facilities doctrine. 8.3. The adoption of the essential facilities doctrine in Europe. 8.4. The limitations of the essential facilities doctrine. 8.5. Refusals to grant network access. 8.6. Conclusions.

8.1. INTRODUCTION.

146. Competition Law and network access. The innovative interpretation of the EC Treaty by the Community competition authorities has often allowed them to lead the process of liberalisation of the European markets. Such was the case with the elimination of the exclusive rights in the telecommunications sector through Directives based on Article 86 EC Treaty (former 90). In parallel, Community competition authorities have been

developing for a decade mechanisms against refusals to grant access to the liberalised networks based on the Community rules on competition.[390]

Such mechanisms departed from the traditional competition principle according to which a refusal to deal by a dominant undertaking would in certain conditions amount to an abuse of dominance prohibited by Article 82 EC Treaty (former Article 86). The transplant of the American essential facilities doctrine tried to strengthen the application of Article 82 to the refusals to grant network access. Nevertheless, these tendencies underline the contradictory nature of the Community rules on competition, as entail a regulatory approach to market power rather than an approach based on the mechanisms which differentiate competition Law.

8.2. THE US ORIGIN OF THE ESSENTIAL FACILITIES DOCTRINE.

147. Refusals to deal in the US. "In the absence of any purpose to create or maintain a monopoly, the [Sherman Act] does not restrict the long-recognised right of a trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal".[391] Such a statement in *United States v. Colgate* at the beginning of the century summarises the key points of the approach to refusals to deal in American antitrust. Section 2 of the Sherman Act does not have the scope of directly protecting the monopolists' clients or competitors through the definition of an obligation to deal, or the consequent prescriptive obligation to deal in fair conditions, imposed on the operators with market power. On the contrary, antitrust is limited to proscribe only behaviours that restrict

[390] This approach has led some authors even to refer to a "new competition Law", see LAROUCHE, P. (2000): "*Competition Law and Regulation in European Telecommunications*", Hart, Oxford.

[391] *United States v. Colgate* 250 U.S. 300, 307 (1919).

competition, understood not as mere rivalry, but as the mechanism which promotes the reduction of prices and the increase of output for the benefit of consumers

At the very same core of American antitrust is a determination not to regulate the exercise of market power but to introduce barriers to the creation of such power. This is based on the assumption that once market power is reached, it is difficult to directly control it, and that exploitation opens space for new competitors to enter the market. As a result, the damage caused by a monopolist to a traditional client by its refusal to deal is not considered itself contrary to the Sherman Act. More willingly, such an abuse might facilitate the emergence of competition and therefore promotes the erosion of market power without requiring a complicated public intervention.[392]

Furthermore, American Courts have been increasingly reluctant to certify the exclusionary effects of refusals to deal. Firstly, it has been commonly accepted that "it is difficult to see how denying a facility to one who [...] is not an actual or potential competitor could enhance or reinforce the monopolist's market power".[393] Secondly, and as a result of the influence of the Chicago School doctrine[394], it has been widely recognise that refusals to deal, even if they damage competitors, might prove pro-competitive if they increase efficiency. The elimination of competitors, particularly in the case of internal vertical integration, does not necessarily suppose the elimination of competition and might on the contrary enhance efficiency, which benefits consumers. For this reason, undertakings accused of monopolising markets

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[392] "Every time the monopolist asserts its market dominance by refusing to supply a firm with some good or service, that firm has more incentive to find an alternative supplier, which in turn gives alternate suppliers more reason to think that they can compete with the monopolist", *Alaska Airlanes v. United Airlanes*, 948 F.2d 536, 549 (9th Cir. 1991), cert. denied, 503 U.S. 977 (1992). See also GLAZER, K. and LIPSKY, A. (1995): "Unilateral Refusals to Deal Under Section 2 of the Sherman Act", in *Antitrust Law Journal*, vol. 63, p. 783.

[393] *Interface Group Inc. v. Massachussets Port Authority*, 816 F.2d 9, 12 (1st Cir. 1987).

[394] *Vide supra* Chapter 2.2. Origins and Evolution of Antitrust.

through refusals to deal should always have the opportunity to allege objective justification to their behaviour. Objective justification do not only comprise situations in which dealing with a competitor might cause direct harm to the undertaking (as is the case with credit-risk companies), but also situations in which dealing with a competitor excludes the efficiency gains derived, for example, from economies of scale or scope.

As a conclusion, refusals to deal are considered contrary to Section 2 of the Sherman Act when such a behaviour despises profit opportunities and imposes costs on the monopolist in order to impose greater costs on the competitors with the result of reducing competition and allowing the monopolist to raise prices and diminish output.[395]

148. The essential facilities doctrine. It has been observed that in some exceptional cases, physical, legal or economic barriers exclude the existence of competition for the production of certain assets. What is more, the monopolistic providers of such assets might have the occasion to expand vertically their position by their refusal to deal with the upstream or downstream competitors that have a vital need for the monopolised asset.

The basic antitrust assumption that competition will erode market power if it is abused is not valid in these cases, as different barriers obstruct the emergence of competition. Therefore, the traditional antitrust approach to refusals to deal does not provide an effective solution to these situations. The essential facilities doctrine appears in this environment in order to impose on the monopolist the prescriptive obligation to provide access to the essential

[395] See FOX, E. (1982): "Monopolization and Dominance in the United States and the European Community: Efficiency, Opportunity, and Fairness", in *Notre Dame Law Review*, vol. 61, pp. 1000-1001. Leading cases as regards refusals to deal are *Eastman Kodak Co. v. Southern Photo Materials Co.*, 273 U.S. 359 (1927); *United States v. Griffith*, 334 U.S. 100 (1948); *Lorain Journal Co. v. United States*, 342 U.S. 143 (1951); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585 (1985); *Eastman Kodak Co. v. Image Technical Services Inc.*, 112 S. Ct. 2072 (1992).

asset in order to make competition possible at least in the vertically connected markets.

The first precedent of the essential facilities doctrine might be traced to a case at the beginning of the century, *Terminal Railroad*,[396] which involved the control by a consortium of railroad operators of a vital junction point in Saint Louis. The Court imposed on the Consortium the obligation to admit rivals to the combination. A similar solution was provided in a case involving a combination for the exchange of information between newspapers, *Associated Press*,[397] even if the lower court had opted to rely on the traditional Common Law obligation to serve everyone imposed on public callings. However, it is *Otter Tail*[398] the first case in which the essential facilities doctrine was applied to a unilateral refusal to deal. The monopolistic provider of electric transmission lines refused to supply power to municipalities developing their own retail distribution networks, and was subsequently condemned for the use of its strategic dominance for maintaining its monopoly by shutting out potential competition.

The expression "essential facilities" was not explicitly used by a court until 1978,[399] and has never been backed by the Supreme Court. However, in the last decades, a substantial case law has developed. The lack of a clear position by the Supreme Court has allowed the coexistence of judgements

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[396] *United Stares v. Terminal Railroad Association*, 224 U.S. 383 (1912). See, nevertheless, a challenging view in REIFFEN, D. and KLEIT, A.N. (1990): "*Terminal Railroad Revisited: Foreclosure of an Essential Facility or simple horizontal Monopoly?*", in *Journal of Law & Economics*, vol. 33, p. 419.

[397] *Associated Press v. United States*, 326 U.S. 1 (1945).

[398] *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973). See an analysis in WERDEN, G.J. (1987): "*The Law and Economics of the Essential Facilities Doctrine*", in *Saint Louis University Law Journal*, vol. 32, p. 461.

[399] *Hecht v. Pro-Football Inc.*, 570 F2d. 982 U.S. 956 (1978). In this case the essential facility was a football stadium.

which have stressed the exceptionality of the doctrine as *MCI v. AT&T*,[400] with judgements which seem to adopt a more flexible approach, such as *Aspen Skiing*.[401]

In any case, some fundamental lines seem to emerge with regard to the applicability of the essential facilities doctrine. Firstly the facility (understood in a very broad sense as any resource, physical or immaterial) must be essential. That means that the resource is vital for the downstream competitor in the sense that the competitor cannot integrate vertically itself and produce the asset, or expect that another undertaking will provide the asset, as it is not possible to duplicate it, and also in the sense that it would not be possible to produce its product without it. Secondly, the obligation to provide the facility should be able to introduce effective competition in the downstream market, what excludes discriminations that lead to such effect. Finally, access to the facility by the downstream competitors has to be physically and economically possible, and competitors have to pay for such access.[402]

149. The exceptional character of the essential facilities doctrine. Different authors have underlined the exceptional character of the essential facilities doctrine in the American antitrust system, and some of them have even expressed the opinion that it should be eliminated.[403] The fundamental criticism is that "since the only qualifying exclusionary practice is the refusal to share itself, the doctrine comes about as close as antitrust ever does to

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[400] *MCI Communications v. American Telephone & Telegraph*, 609 F2d 843 (6th Cir 1979). Also *Mckenzie v. Mercy Hospital*, 854 F.2d 365 (10th Cir. 1988); or *City of Anaheim v. Southern California Edison Co.*, 955 F.2d 1373 (9th Cir. 1992).

[401] *Vide supra* footnote 395.

[402] See VENIT, J. and KALLAUGHER, J. (1994): "Essential Facilities: A Comparative Law Approach", in "*Annual Proceedings of the Fordham Corporate Law Institute*", pp. 322-324.

[403] See AREEDA, P. (1990): "Essential Facilities: An Epithet in Need of Limiting Principles", in *Antitrust Law* Journal, vol. 58, pp. 852-853; AREEDA, P. and HOVENKAMP, H. (1996): "*Antitrust Law. An Analysis of Antitrust Principles and Their Application*", vol. III.1, Little Brown, Boston, p. 172; WERDEN (1987), p. 480 (supra footnote 398).

condemning 'no fault' monopolisation".[404] That is, the essential facilities doctrine focuses the attention not in the process of development of the monopolistic position, but in the fairness of behaviour of the monopolist itself, without considering the objective justification which could be provided by the monopolist. The essential facilities doctrine acquires therefore a regulatory nature that seems incompatible with the principles of American antitrust.

The essential facilities doctrine has a close connection with the Common Law tradition of the common calling, and the connected obligation to serve all at a reasonable rate with no discrimination derived from the public interest of certain activities.[405] As a matter of fact, it has been pointed that in *Associated Press* the lower court based its decision on the traditional Common Law obligations which informed an activity clothed with a public interest as journalism. Even if the Supreme Court stated expressly that it was not applying a public utility concept, a member of the Supreme Court recognised that the judgement would not decide the considerable question on whether compulsory dealing would be an appropriate Sherman Act remedy or should await further legislative action.[406]

Rather than preventing monopolisation through the proscription of exclusionary practices, the essential facilities doctrine regulates the behaviour of the monopolist through the prescription of the rules governing its relation with the downstream competitors. In the original cases of collective refusals to deal, antitrust intervention required no more than a prohibition of the refusal to put an end to the anticompetitive behaviour.

The expansion of the figure to unilateral refusals to provide access to an essential facility modifies the nature of the intervention from proscriptive to

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[404] *Ibid.* AREEDA and HOVENKAMP (1996), p. 176: "the 'essential facility' doctrine is both harmful and unnecessary and should be abandoned".

[405] *Vide supra* Chapter 2.1. Origins and Evolution of Economic Regulation.

prescriptive, as the permanence of the market power of the monopolist requires antitrust authorities to define all the conditions of the provision and particularly the pricing and the non-discrimination in the provision.

It has already been pointed out that antitrust authorities lack the mechanisms to undertake such a task. It is for this reason that a number of authors have proposed to apply the essential facilities doctrine exclusively in those cases in which a regulatory framework is in place and where it defines the prescriptive rules governing the monopolised activity.[407] Such was the case for instance in *Otter Tail* or *MCI v. AT&T*. The essential facilities doctrine would then play a mere complementary role.

As a conclusion, the essential facilities doctrine, even if limited to the clearest cases of unavoidable vertically integrated monopoly, supposes the introduction of a regulatory figure in the American antitrust system. Such a figure is incompatible with the general principles which inform antitrust, as well as with the mechanisms provided for ensuring the effectivity of such principles, unless applied in close co-ordination with the existing regulatory framework.

8.3. THE ADOPTION OF THE ESSENTIAL FACILITIES DOCTRINE IN EUROPE.

150. Essential facilities in Europe. The essential facilities doctrine has been transplanted from American antitrust to European competition Law by the

[406] *Vide Associated Press v. United States*, p. 25 (*supra* footnote 397).

[407] *Vide* AREEDA and HOVENKAMP (1996) p. 201 (*supra* footnote 403), and EDGARD, F. (1993): "The Essential Facilities Doctrine and Public Utilities: Another Layer of regulation?", in *Idaho Law Review*, vol. 29, no. 2, p. 311.

European competition authorities (initially by the Community authorities but followed early by the national counterparts).[408]

It is evident that the situation that has given rise to the development of the doctrine in the US was also faced in Europe, and that American antitrust has always been the model of reference for European competition Law. It might not be so evident, but it seems to be the case that the essential facilities doctrine is far more compatible with the European antitrust tradition than with the American tradition. The former has been always characterised by an approach based on the fairness of the monopolist behaviour and the regulatory character of the intervention against monopolists' abuses.[409] Maybe for this reason it has been repeatedly argued that the doctrine does not introduce a significant novelty in the European system. What has not been commonly recognised, however, is that the transplant of the doctrine underlines the most basic inconsistencies of the policy towards market power.

151. A doctrine compatible with the traditional approach. The regulatory approach of the European rules on abuse of dominant position decisively influenced the early development of the refusals to deal category. Even if this behaviour is not explicitly defined in Article 82 EC Treaty, the

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[408] See different commentaries on refusals to deal and essential facilities in BROKELMANN, H. (1997): "Las negativas de suministro en el Derecho de la competencia comunitario y español", in *Gaceta Jurídica de la C.E. y de la Competencia*, B-125, pp. 5-26; CAZZOLA, C. (1999): "La dottrina dell'essential facilities e la politica antitrust", in "La disciplina giuridica della telecomunicazioni", Giuffre, Milano, pp. 219-259; FURSE, M. (1995): "The 'Essential Facilities' Doctrine in Community Law", in *European Competition Law Review*, vol. 8, pp. 469-473; GLASL, D. (1994): "Essential Facilities Doctrine in EC Anti-trust Law: A Contribution to the Current Debate", in *European Competition Law Review*, vol. 15, no. 6, pp. 306-314; LAROUCHE, P. (2000): "*Competition Law and Regulation in European Telecommunications*", Hart, Oxford, 179-217; RIDYARD, D. (1996): "Essential Facilities and the Obligation to Supply Competitors under UK and EC Competition Law", in *European Competition Law Review*, vol. 17, no. 8, pp. 438-452; SUBIOTTO, R. (1992): "The Right to Deal with Whom One Pleases under EEC Competition Law: A Small Contribution to a Necessary Debate", in *European Competition Law Review*, vol. 13, no. 6, pp. 234-244; TEMPLE LANG, J. (1989): "Defining Legitimate Competition: Companies' Duties to Supply Competitors, and Access to Essential Facilities", in "*Annual Proceedings of the Fordham Corporate Law Institute*", pp. 245-313; VENIT, J. and KALLAUGHER, J. (1994): "Essential Facilities: A Comparative Law Approach", in "*Annual Proceedings of the Fordham Corporate Law Institute*", pp. 315-343.

[409] *Vide supra* Chapter 3.2. Competition Law in Europe.

Community competition authorities judged that refusals to deal were implicitly included under the abusive behaviours prohibited generically by Article 82 or even expressly under letters a), b) and even c). It was particularly the American authors[410] who pointed out that refusals to deal were not prohibited because of their effect on competition, but rather because of the lack of fairness with regard to the relationship between the undertaking in a dominant position and its clients and competitors.

The main concern of the European Court of Justice in early cases of refusal to deal such as *United Brands*,[411] was the unfairness for the traditional distributors of the unilateral refusal to deal by the dominant undertakings due to the exploitative nature of such a behaviour. As a matter of fact, the ECJ stated that the lack of a consolidated relationship excluded the abusive character of the refusal of BP to provide its services to ABG during a petrol shortage.[412] It was absolutely irrelevant whether there was a competitive relation between the undertakings, as the unfairness had its origin in the betrayed trust of a traditional customer, and not in the anticompetitive nature of the behaviour. In this way, it became a principle of competition policy that the refusal to deal to a traditional customer by a dominant undertaking would amount to an abusive behaviour.

The expansion in the application of Article 82 from exploitative behaviours to also include exclusionary behaviours increased the initially timid intervention against market power. Nevertheless, the regulatory nature of the control of the fairness of the dominant undertaking's behaviour predominated over efficiency considerations, sometimes due to parallel objectives on the

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[410] See KAUPER, T. (1989): "Whither Article 82? Observations on Excessive Prices and Refusals to Deal", in "*Annual Proceedings of the Fordham Corporate Law Institute*", pp. 651-682; and FOX, E. (1982): "Monopolization and Dominance in the United States and the European Community: Efficiency, Opportunity, and Fairness", in *Notre Dame Law Review*, vol. 61, pp. 981-1020.

[411] *United Brands v. Commission*, Case 27/76, 1978 ECR 207.

[412] *British Petroleum v. Commission*, Case 77/77, 1978 ECR 1513.

rules on competition such as market integration. As a result, the inconsistencies which had little effect under a little applied provision produced major interferences when they were expanded to a much broader set of situations.

A good example of this phenomenon can be appreciated with regard to refusals to deal. Cases such as *Commercial Solvents*[413] show that the European competition authorities were more focused on the unfair effects of refusals to deal on the competitor eliminated from the market due to the vertical integration of Commercial Solvents than on the effects on competition and consumer welfare. Actually, Commercial Solvents' refusal to deal probably did not reduce competition, but merely substituted one competitor for another involved in a process of vertical integration which could have been proved more efficient and beneficial for the consumers thanks to the integration. The Court, however, never balanced such effects, as it only focused on the unfairness for the competitor.

Furthermore, in *Telemarketing*[414] and *GB-Inno-BM*,[415] the Court refused to accept the defendant's argument that the refusal to deal would only be abusive if it threatened harm to consumers through increases of prices or other negative effects.[416] On the contrary, the principle was established that "an abuse within the meaning of Article 86 [now 82] is committed where, without any objective necessity, an undertaking holding a dominant position on a particular market reserves for itself an ancillary activity which might be carried out by another undertaking as part of its activities on a neighbouring but separate market, with the possibility of eliminating all competition from such undertaking".[417]

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[413] *Commercial Solvents v. Commission*, Cases 6 and 7/73, 1974 ECR 223.

[414] *CBEM v. CLT*, Case 311/84, 1985 ECR 3261.

[415] *GB-Inno-BM*, Case C-18/88, 1991 ECR I-5941.

[416] *Vide* FOX (1982), p. 998 (*supra* footnote 410).

[417] *Vide GB-Inno-BM*, para. 18 (*supra* footnote 415).

152. Exploitation, exclusion, efficiency and uncertainty. As the application of Article 82 EC Treaty to the obstruction of exclusionary abuses was confirmed, a new strand of Commission decisions on refusals to deal appeared, more focused on the effects on competition of such refusal than on the effects on the competitors. Some signs of such a shift can be identified in *Boosey and Hawkes*.[418]

More clearly, the Commission stated in *British Midland/Aer Lingus* that "Aer Lingus has not been able to point to efficiencies created by a refusal to interline nor to advance any other persuasive and legitimate business justification for its conduct",[419] and for this reason declared anticompetitive the refusal to reach an interlining agreement with the new comer and it therefore was excluded from the market. In a similar way, the Commission in *London European/Sabena*[420] stressed the fact that the dominant carrier's refusal to grant access to the leading computerised reservation system not only excluded London European from the market, but also allowed the dominant carrier to keep prices up, causing harm to the consumer.

An evolution of the Community institutions from a purely exploitative approach to a cumulative exclusionary approach and later to an evaluation of the exclusionary effects in line with American Section 2 of the Sherman Act, can therefore be identified. The result was an extremely confusing mixture of exploitative and exclusionary abuses, complicated by the introduction of the efficiency argument. As an example, the three well known behaviours defined by the Court in *Volvo/Veng*[421] as abuses of a dominant position derived from an intellectual property right, mixed all these elements as it defined at the same

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[418] *Bookey and Hawkes*, Commission Decision 87/500/EEC, OJ L 282/36 of 29.7.87. For an analysis on these lines *vide* KAUPER (1982), pp. 678-679 (*supra* footnote 410).

[419] *British Midland/Aer Lingus*, Commission Decision 92/213/EEC, OJ L 96/32, OJ 1992

[420] *London European/Sabena*, Commission Decision 88/589/EEC, OJ L 317/47 of 24.11.88.

[421] *AB Volvo v. Erik Veng UK Ltd.*, Case 238/87, 1988 ERC 6211.

level unfair practices related to excessive pricing, absolute refusals to deal and anticompetitive behaviours affecting efficiency.

The essential facilities, easily adaptable to the European approach to market power, was introduced by the European Commission at that moment in order to face the lack of coherent rules for the treatment of refusals to deal, and in particular to obstruct refusals to deal to new customers. The requirements developed by the lower American courts for the application of the doctrine, particularly in *MCI v. AT&T*,[422] provided the necessary instruments for analysing refusals and to limit the application of a figure which obviously required precise limits in order to avoid the excessive intervention imposing access to existing facilities.

153. Early cases. The very first case in which European institutions expressly mentioned the doctrine of the essential facilities was in the granting of interim measures by the Commission in the case *B&I/Sealink*.[423] In a very similar case related also to the exploitation of ports, *Sea Continers/Stena Sealink*,[424] the Commission stated that "an undertaking which occupies a dominant position in the provision of an essential facility and itself uses that facility (i.e., a facility or infrastructure, without access to which competitors cannot provide services to their customers), and which refuses other companies access to that facility without objective justification or grants access to competitors only in terms less favourable than those which it gives to its own services, infringes Article 86 [now 82] if the other conditions of that Article are met".[425]

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[422] *Vide supra* footnote 400.

[423] *B&I Line plc v. Stena Sea Link*, Commission Decision of 11 June 1992.

[424] *Sea Continers/Stena Sea Link*, Commission Decision 94/19/EC OJ L 15/8 of 18.1.94.

[425] *Ibid.* para. 66.

Even if the Commission transplanted the expression "essential facilities" and most of the requirements defined by American courts (vertical integration, essentiality and the refusal of discriminatory contracting), the decision lacked a clear delimitation of the conditions that define a facility as essential. In the US the essential facilities doctrine has been widely recognised as an exceptional solution for very exceptional situations in which competition, for some reason is excluded from a particular market. The first decisions of the Commission under the cover of the essential facilities, on the contrary, failed to identify the exceptional conditions that made the port of Holyhead an essential facility

As a result, a dangerous precedent was opened both at the Community level and at a national level allowing a flow of requirements by undertakings to have access to the facilities of their competitors, as they understood that a refusal would amount to an abusive exclusionary behaviour prohibited by Article 82 EC Treaty. For instance, the requirement of small competitors to have access to the distribution channels of competitors enjoying a dominant position became common, as it was argued that small competitors would otherwise have no place on the market.[426]

The Court's decision in *Magill*[427] increased the uncertainty due to the fact that for the first time, the obligation to renounce to the exclusivity it entails was imposed on the holder of an intellectual right. At the same time, the case introduced the novelty of imposing the obligation to deal with an undertaking that had never been a client of the holders of the exclusive right.

The legal certainty which emerged from the clear separation between the antitrust and the regulatory intervention was also damaged by the tendency of the Commission to introduce regulatory obligations in the exercise of its

[426] See for instance the case *Tabacalera* under the Spanish competition authorities, commented in BROKELMAN (1997), pp. 24-26 (*vide supra* footnote 408).

[427] *RTE and ITP v. Commission*, Case 242/91, 1995 ECR I-743.

antitrust competencies. It became increasingly common to impose regulatory obligations on the undertakings notifying concentrative or co-operative joint-ventures in relation to access to essential facilities as conditions for the approval of the operation under the merger regulation or under Article 81(3). Such a practice has been common not only in the telecommunications industry,[428] but also in other network industries as air transportation[429] or railroads.[430]

In conclusion, the introduction of the essential facilities doctrine by the European Commission without a clear definition of the conditions required to apply such an exceptional intervention, caused legal uncertainty. The reason was that undertakings heavily investing in R&D, in the installation of infrastructures, or in general, in the development of assets which would provide a competitive advantage as a result of the more efficient response to the consumer's demands, were menace to share with their competitors their competitive advantage.

154. Latest case law. The dangerous door opened by the Commission by an insufficiently precise transplant of the American essential facilities doctrine has been recently closed (even if not locked) by the Community courts. A number of decisive judgements have established strict requirements for the definition of a facility as essential, and have limited the role of the Commission as a regulator.

The first important judgement was delivered by the Court of First Instance in *Ladbroke v. Commission*.[431] The Court stated that the refusal by the holder of the exclusive rights for television images on French horse racing to

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[428] Worldcom/MCI, Commission Decision Case IV/M.1069, of 8.7.98.

[429] *Swissair/Sabena II*, Commission Decision Case IV/M.616 of 20.7.95.

[430] *European Night Services*, Commission Decision 94/663/EC, OJ L 259/10, of 21.9.94.

[431] *Tiercé Ladbroke v. Commission*, Case T-504/93, 1997 ECR II-923.

grant access to such images to an undertaking running betting shops in Belgium was not contrary to Article 82 EC Treaty. The main reason was that the French undertaking was not present in the Belgium market, and since no competition existed between them, no exclusionary practice was possible. This judgement can be interpreted along the lines of separating exploitative from exclusionary abuses with regard to refusals to deal.

Another interesting judgement was delivered by the Court of First Instance in the case *European Night Services*.[432] The Court annulled a Commission Decision relating to a proceeding pursuant to Article 81 of the EC Treaty. It was considered, among other grounds, that the Commission had failed to demonstrate the necessity of imposing on the parties involved in a co-operative joint venture for the running of a night railroad service across the Channel, the obligation to supply train paths, locomotives and crews to third parties on the same terms as to the joint-venture company. The Court considered that, as train paths are concerned, an existing Directive already imposed such an obligation, in such a way that the agreement could not, by definition, restrict it. Thus, it was restricted the regulatory character of the Commission intervention in application of the rules on competition in favour of the regular regulatory channels. As regards locomotives and crews, the Court stated that the essentiality of the facilities was never demonstrated. Furthermore, the Court stated that the fact that the notifying parties were the first ones to acquire such facilities, and for a period the only ones, did not imply that they are alone in being able to do so.

Finally, it is decisive the judgement of the European Court of Justice in *Oscar Bronner*,[433] following the lines of a detailed reasoned opinion of

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[432] *European Night Services v. Commission*, Joint Cases T-374, 375, 384 and 288/94, 1998 ECR II-3141.

[433] *Oscar Bronner v. Mediaprint*, Case C-7/97, 1998 ECR I-7791. Comments in LAROUCHE (2000), pp. 193-196 (*vide supra* footnote 408);

Advocate General Jacobs. The ECJ established the requirements for considering a refusal to grant access to an essential facility contrary to Article 82 EC Treaty. In so doing, the exceptional character of the American doctrine was also introduced in European competition Law.

The first requirement for the consideration of the obligation to grant access is the finding of the essential character of a facility. Such essentiality, as in the American case, has a double sense. On the one hand, and this is the centre of the doctrine, there has to be an insurmountable barrier to duplicate the facility. "That might be the case for example where duplication of the facility is impossible or extremely difficult owing to physical, geographical or legal constraints or is highly undesirable for reasons of public policy".[434] It might also be the case, as the Advocate General Jacobs points out, due to economic reasons, and the fact that the facility was developed under no-competitive reasons or that the economies of scale make the development of an alternative facility uneconomic. In any case, the impossibility to duplicate the facility has to be objective. Therefore, it is not limited to the impossibility for a specific downstream competitor to integrate vertically due to its small size, but to the impossibility faced by any potential competitor to introduce effective competition in the upstream market. On the other hand, the facility has to be "indispensable to carrying on that person's [the downstream operator] business".[435]

Secondly, in order to dictate a breach of Article 82 EC Treaty, the refusal has to be "incapable of being objectively justified".[436] The Court does not elaborate more on this point, but it is clear that such circumstances as the credit-risk character of the potential client justify the refusal to deal. The key point is whether objective justifications based on grounds of efficiency could

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[434] *Ibid.* Opinion of the Advocate General, para. 64.

[435] *Ibid.* para. 41.

be accepted. Advocate General Jacobs points out that it may be the case in the US, but it seems that is in the very same essence of the doctrine in the US that the monopolistic nature of the market of the facility excludes the possibility of considering efficiency justifications, as the consumer would never benefit from them due to the lack even of potential competition on the monopolist. The same reasoning could be applied in Europe. Actually, this might be the centre of the essential facilities doctrine and the difference against the regular refusal to deal, where objective justifications based on efficiency have to be considered.

Finally, the Court required that the refusal of the service be likely to eliminate all competition in the downstream market. In the case of essential facilities, as they have been qualified by the court, this will unavoidably be the case, and for this reason they are an abuse of Article 82 EC Treaty *per se*. Some American authors have proposed to strengthen this requirement so that access is provided not only when refusal eliminates all competition, but also when such access would substantially improve competition in the downstream market.[437]

8.4. THE LIMITATIONS OF THE ESSENTIAL FACILITIES DOCTRINE.

155. Conclusions regarding access to essential facilities. The judgements of the Community courts on essential facilities have clarified the role of the American doctrine in European competition Law. The European Court of Justice has imposed a more restrictive approach to essential facilities than the European Commission. In this way, the exceptional character of the treatment reserved for those markets in which no competition is possible and the monopoly could be expanded to vertically related markets, has been

[436] *Ibid.* Judgement of the Court, para. 41

[437] *Vide* AREEDA and HOVEMLAMP (1996) p. 200 (*supra* footnote 403).

transplanted to Europe. As a result and, it has to be stressed again, exceptionally, "a dominant undertaking must not merely refrain from anti-competitive action but must actively promote competition by allowing potential competitors access to the facilities which it has developed".[438]

Furthermore, the Court of First Instance has also limited the regulatory intervention of the Commission in the application of the rules on competition. As a matter of fact, it has underlined the lack of necessity of conditioning to the provision of access to a facility in the necessary approval of joint ventures under Article 81(3) if such obligation has already been introduced by a Community Directive. At the same time, it has also imposed exceptional standards to the introduction of such conditions in case no regulatory obligation exists.

The courts, nevertheless, have not yet stated their position regarding the conditions in which access to essential facilities has to be granted. American literature has pointed out the regulatory character of the essential facilities doctrine, and the inconsistencies of besting on the competition authorities the definition of the conditions of access without the attribution of the necessary mechanisms.[439] Such problems are even more relevant in the European case due to the traditional regulatory character of Article 82 EC Treaty and the mixture between exploitative, exclusionary and efficiency considerations in the application of such provision to refusals to deal.

Deriving from the very same nature of the essential facilities doctrine is the notion that access by third parties to such facilities has to be granted at the same conditions at which the vertically integrated monopolist enjoys them.[440]

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[438] *Vide Oscar Bronner*, Resoned Opinion of the Advocate General, para. 34 (*supra* footnote 433). This has been also pointed in LAROUCHE (2000) p. 209 (*vide supra* footnote 408).

[439] *Vide* ARREDA and HOVENKAMP (1996), pp. 166-172 (*supra* footnote 403); and LAROUCHE (2000), p. 210 (*supra* footnote 408).

[440] *Vide* analysis in LAROUCHE (2000), pp. 218-231 (*supra* footnote 408).

Otherwise, downstream competitors would never be in the position to compete and the discriminatory conditions would amount to a refusal to deal that is considered unlawful. This is shared by American antitrust and European competition Law. In the simplest cases the mere obligation to provide non-discriminatory access might be enough to regulate access conditions. Vertical integration, particularly in industries with a predominance of the common versus the specific costs, however, might often complicate the comparison of the conditions, particularly the price, at which access is provided to all the undertakings active in the downstream market.

A further problem in Europe derives from the possible interference of the traditional fairness approach regarding market power in the definition of access conditions. As a matter of fact, the Commission made clear its intentions to link access to essential facilities to traditional case law, for instance on production limitation and even on excessive pricing.[441] This approach would definitely take the essential facilities doctrine to a clearly regulatory field that is excluded in the US.[442] Competition is not necessarily limited in the downstream market if both competitors and the vertically integrated division of the monopolist suffer the same prices for the utilisation of the essential facility, even if such prices are definitely over the cost of production. In any event, such a regulatory intervention would risk lack of effectivity, due to the lack of adaptation of the mechanisms provided by the rules on competition.

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[441] Notice on the application of the competition rules to access agreements in the telecommunications sector. Framework, relevant markets and principles, OJ C 265/2 of 22.8.98, para. 105-109.

[442] Advocate General Jacobs in his brilliant reasoned opinion in *Oscar Bronner*, para. 47 (*vide supra* footnote 433) relies on one of the earliest American precedent on refusals to deal, *Eastman Kodak v. Southern Photo Materials* (*vide supra* footnote 395) in order to suggest that in the US the essential facilities doctrine would include the obligation to contract on reasonable terms. Nevertheless, such position seems incompatible with the evolution of American antitrust particularly after the influence of the Chicago School, as it is underlined for instance by ARREDA and HOVEMKAMP (1996) pp. 167-228 (*vide supra* footnote 403) and GLAZER and LIPSKY (1995), pp. 749-800 (*vide supra* footnote 392). Advocate General Jacobs seems to suggest the convenience to allow the monopolist producer of an essential facility to recover the heavy investments through temporary monopolistic pricing. This option would force competition authorities to adopt a complicated 'rate of return' regulation.

For all these reasons, the essential facilities doctrine, both in the US, but particularly in Europe, requires the co-ordination with other public intervention instruments, and particularly economic regulation, as the latest instrument disposes of mechanisms such as the imposition of specific proscriptive obligations which allow firstly for the clarification of the conditions of access to the facility by the vertically integrated division of the monopolist (through accounts separation, for instance) and secondly for setting out the specific conditions under which access should take place.

156. Conclusion as regards access to non-essential facilities. The debate on the introduction of the essential facilities doctrine and the position of the European Courts not only have clarified the principles ruling access to these facilities, but also have developed the reflection on the general category of refusals to deal and might force competition authorities to adopt a stricter approach regarding access to non-essential facilities.

The reflections of Advocate General Jacobs confirm the introduction in the European debate about refusal to deal of a series of principles that have not always led the application of Article 82 by the European competition authorities. It is now firmly established not only that "the right to chose one's trading partner and freely to dispose of one's property are generally recognised principles in the laws of the Member States",[443] but also that "in the long term is generally pro-competitive and in the interest of consumers to allow a company to retain for its own use facilities which it has developed for the purposes of its business. [...] Thus the mere fact that by retaining a facility for its own use a dominant undertaking retains an advantage over a competitor cannot justify requiring access to it".[444]

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[443] Advocate General reasoned opinion in *Oscar Bronner*, para. 56 (*vide supra* footnote 433).

[444] *Ibid.* para. 57.

Advocate General Jacobs states with absolute clarity the main principles which should rule refusals to deal: "the primary purpose of Article 86 [now Article 82] is to prevent distortion of competition [...] rather than to protect the position of particular competitors. It may therefore [...] be unsatisfactory, in a case in which a competitor demands access to a raw material in order to be able to compete with the dominant undertaking on a downstream market in a final product, to focus solely on the latter's market power on the upstream market power and conclude that its conduct in reserving to itself the downstream market is automatically an abuse. Such conduct will not have an adverse impact on consumers unless the dominant undertaking's final product is sufficiently insulated from competition to give it market power".[445]

Only in the case of essential facilities does the mere refusal to deal *per se* excludes the existence of competition in the downstream market due to the exceptional vital character of these facilities. For the rest of facilities, as a result, it will be necessary to identify circumstances which, in parallel to the refusal to deal exclude competition in the downstream market and therefor damage competition for the final product.

The test should not be centred on the existence of a mere refusal but whether such refusal despises profit opportunities and imposes costs on the monopolist in order to impose greater costs on the competitors with the result of reducing competition and allowing the monopolist to raise prices and diminish output.

In case the refusal to deal affects a competitor in a vertically related market, the interest of the consumer should be protected over the interest of the competitors. Mere damage to the competitors, even the elimination of a particular competitor, should not be considered itself an abuse. It should be as

[445] *Ibid.* para. 58.

well necessary to determine whether damage to downstream competitors is balanced by increases in efficiency by the vertically integrated undertaking and by the benefits obtained by consumers out of this efficiency. This balance should not be contaminated by fairness considerations leading to regulatory interventions supposed to benefit consumers in the long run. At the same time, it seems clear that a refusal to deal by an undertaking which is not a competitor in the downstream market cannot be considered exclusionary.[446]

Exploitative abuses should be restricted as much as possible, as they entail a heavy regulatory intervention outside of the scope of the rules on competition. This is particularly true for the refusals to deal with new customers. In the case of traditional customers, the rules on competition can provide a simple solution by forcing the dominant operator to restore the traditional conditions of access. In the case of new customers such a solution is more complicated, particularly if no other undertaking has access to the facility and it is necessary not only to require access but unavoidably also access conditions.

8.5. REFUSALS TO GRANT NETWORK ACCESS.

8.5.1. General Considerations.

157. Introduction. It is not simple to adapt the analysed approach to refusals to deal to the specific circumstances of the telecommunications sector. It is not simple firstly because the approach itself is far from being clear, as it is evolving in part due to the pressure to find effective solutions for access in

[446] Of course, a refusal to deal with an undertaking in a downstream market where the provider is not present could have the purpose of excluding from the market a direct competitor in the upstream market with whom the dominant undertaking does not want its client to deal. In this case a horizontal exclusionary effect can be identified even if the direct effects are suffered by the company in the downstream market. This was the case in *Loraine* (*vide supra* footnote 395) and also in *United Brands* (*vide supra* footnote 411).

liberalised network industries. Furthermore, the character of industry in transition complicates the definition of relevant markets and the evaluation of the economic characteristics of such markets.

The Notice on the application of the competition rules to access agreements in the telecommunications sector[447] was supposed to set out the principles stemming from Community competition Law regarding access in the telecommunications sector, in order to introduce legal certainty and stable conditions for investment. The Commission elaborated on the traditional judgements of the CFI and the ECJ on refusals to deal as well as on the more abundant and aggressive Commission decisions, particularly on those that had introduced the essential facilities doctrine. Besides this, the Commission advanced some of the new principles that would rule its intervention in the telecommunications sector.

The essential facilities doctrine, as it had been developed by the Commission throughout its case law, played a decisive role in the whole system. However, the posterior intervention of the European Courts has introduced an element of doubt about the validity of certain assumptions of the Commission reflected in the Access Notice.

8.5.2. The Access Notice.

158. The Access Notice. The Commission's analysis departed from the recognition of the relevance of access in the telecommunications sector. The double factual monopoly enjoyed by the vertically integrated incumbents, both in the infrastructures markets and in the services markets, grants them a

[447] Notice on the application of the competition rules to access agreements in the telecommunications sector. Framework, relevant markets and principles, OJ 1998 C 265/2, of 22.8.98. For comments on it see COATES, K. (1997): "EU Competition Rules and Access Problems in the Telecoms Sector", in *International Business Lawyer*, pp. 310-317; VAN LIEDEKERKE, D. (1997): "European Commission's Draft Notice on Access in the Telecommunications Sector", in *International Business Lawyer*, pp. 318-328.

particularly strong market power. Relying on the traditional *Hoffman-La Roche* formula, the Commission based the potential abusive character of the refusals to give access to the monopolised facilities on the effect of hindering the maintenance of the degree of competition still existing in the market or the growth of that competition.

The Commission's position in the Access Notice, however, might not always be compatible with the case law of the European courts, particularly with the judgements on the essential facility doctrine. On the one hand, the Commission seems to adopt an excessively wide view of the application of the general category of refusals to deal, which has not always been backed by the ECJ. On the other hand, the category of essential facilities, even if more restricted than in some of the early Commission decisions, might still be wider than defined by the ECJ.

It seems to be the case that the Commission, in the Access Notice, diminish the potential role of the essential facilities doctrine and foster the application of the more traditional principles on abusive behaviour, maybe as a result of the criticisms raised by early Commission decisions on essential facilities. The result, though, is an under-utilisation of a doctrine which might be helpful to tackle some issues faced in liberalised network industries, and an over-stretch of the traditional principles on refusal to deal.

159. Withdrawal of access. Three different scenarios are distinguished in the Access Notice in order to evaluate the exploitative or exclusionary effects of the refusals to deal. The simplest scenario is the withdrawal of access from an existing customer.[448] There is substantial case law both from the Commission and from the ECJ which confirms the abusive nature of such behaviour.[449] Simplicity derives also from the fact that this abuse entails

[448] *Ibid.* para. 99-100.

[449] *Vide supra* Chapter 8.3. The Adoption of the Essential Facilities Doctrine in Europe.

predominantly exploitative effects and, therefore, the difficulties originated by the mixture of exploitative and exclusionary effects are avoided, as well as the reflections on the effect on efficiency.

160. Discriminatory refusal to grant access. A second scenario is the refusal to grant access where another operator has been already given access to the same facility. The Commission considers that "it is clear that a refusal to supply a new customer in circumstances where a dominant facilities owner is already supplying one or more customer operating in the same downstream market would constitute discriminatory treatment which, if it would restrict competition on that downstream market, would be an abuse".[450] The Commission considers that this is particularly the case if discrimination benefits the downstream arm of the facilities owner.

What is supposed to be the most common abusive refusal to deal in the telecommunications sector receives little attention in the Access Notice. The Commission merely states that discrimination is abusive if it restricts competition in the downstream market, and that the vertically integrated incumbents have both the opportunity and the incentive to restrict competition. The Commission seems to suggest that all refusals to deal to downstream competitors are abusive unless an objective justification exists, and only quotes credit-risk as an objective justification.

The Commission does not determine under which circumstances discrimination will lead to abuse. Furthermore, the Commission seems to undermine what Advocate General Jacobs, in *Oscar Bronner*, defines as the central element of the whole construction, that is efficiency.[451]

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[450] *Vide* Access Notice para. 85 (*supra* footnote 447).

[451] *Vide supra* Chapter 8.3. The Adoption of the Essential Facilities Doctrine in Europe.

Article 82(c) EC Treaty states that abuses of dominant position might consist in "applying dissimilar conditions to equivalent transactions with other trading partners, thereby placing them at a competitive disadvantage". Such a provision has traditionally been interpreted as a limitation to introduce discriminations between clients, not between the dominant operator and its competitors.[452]

This is a very good example of the vagueness and confusion introduced by the connection between exploitative practices (discrimination) and exclusionary practices (foreclosure). The strategy reflected in the Access Notice relies, once more, on the dangerous combination of exploitative and the exclusionary effects, which usually leads to the reduction of the efficiency considerations.

Concluding, the Commission tries to avoid the most delicate point that is why the mere refusal to deal can be considered abusive even if the facility cannot be considered essential. The reasoning in this point of the Access Notice seems only applicable to essential facilities, but not to non-essential facilities, as in the latest case efficiency consideration should be included among the list of objective justification not to deal

161. Essential facilities. The most elaborated reasoning, based on the essential facilities doctrine, is reserved for the a third scenario, characterised by the refusal to grant access for the purpose of a service where no other operator has been given access by the access provider, not even a downstream arm of the monopolist.[453] The Commission advances five requirements for the imposition of the obligation to grant access.

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[452] *Vide* the analysis in LAROUCHE (2000), p.218-231 (*supra* footnote 408).

[453] *Vide* Access Notice, para. 87-98 (*supra* footnote 447).

Firstly, the facility has to be essential for companies to compete on the related market. The Commission does not elaborate too much on this fundamental point. It states that it is not enough for compulsory access to improve the position of the company. Rather, the proposed activities are made impossible or seriously and unavoidably uneconomic. The Commission recognises that it is not enough to demonstrate that access is necessary for a particular competitor. Nevertheless the Commission approach does not seem to be as objective as the approach of the ECJ in *Oscar Bronner*. While the ECJ seems to impose an absolute impossibility for any competitor, the Commission seems to think that it is enough to "demonstrate that access is necessary for all except for exceptional competitors in order for access to be made compulsory".[454]

Secondly, there has to be enough spare capacity available to provide access. This condition puts an end to the debate generated by the Commission decision in *Port of Rodby,*[455] which allowed certain doctrine to suggest that saturated facilities could be shared in order to introduce some competition in the downstream market.

Thirdly, and this is the other key point of the Commission's construction, the owner of the facility has to fail to satisfy demand, to block the emergence of a potential new service or impede competition on an existing or potential service. As it is put by the Commission "unless access is granted, the party requesting would not be able to operate in the service market. Refusals in this

[454] At this point, it is very interesting to remind ourselves of what is the main criticism of the essential facilities doctrine in LAROUCHE (2000), p. 212 (supra footnote 408): the dominance analysis is substituted by the essentiality analysis, an analysis whose conclusion depends strongly on the market definition, what can lead to baseless intervention.

[455] *Port of Rodby*, Commission Decision 94/119/EEC, OJ L 55/52, of 26.2.94.

case would therefore limit the development of new markets, or new products on those markets, contrary to Article 82(b)".[456]

Finally, the Commission requires two more conditions. On the one hand, the company requesting access has to be prepared to pay for such access. On the other, no objective justification for the refusal exists. The Commission refers to justifications such as the technical difficulty of providing access. It seems clear after the analysis of the judgements of the ECJ, that in this case objective justifications are reduced, as no efficiency argument can be used in case of essential facilities.

This might be an unnecessarily complex approach. According to the position of the ECJ, the mere refusal to grant access to an essential facility is abusive as it forecloses competition in the downstream market. It seems unnecessary to link the exclusionary effect to one of the traditional exploitative effects, mostly when there is no case law supporting the application of such an approach.

8.5.3. A Different Scheme.

162. Essential telecommunications facilities. It seems absolutely necessary, first of all, to consider whether certain telecommunications infrastructures can be considered essential, in order that the essential facilities doctrine can be applied. For the application of the rules on competition, the only valid definition of essential facilities is the developed by the ECJ. Other definitions can have effect in other ambits, for instance the regulatory.[457] Besides, the consideration of a facility as essential can only be undertook case-by-case, as the rules on competition do not provide a mechanism for the

[456] *Vide* Access Notice para. 88 (*supra* footnote 447).

[457] This is the case, for instance, with the definition contained in the Additional commitment on regulatory principles by the European Communities and their Member States in the framework of the WTO negotiations, which seems wider than the definition of the ECJ, as it includes markets where competition exists, even if weak or between a very limited number of players.

consideration *ex ante* and in general terms of a particular infrastructure and, furthermore, as the specific conditions of specific markets have to be evaluated for the application of the rules on competition.

The application of the strict criteria defined by the ECJ in *Oscar Bronner* limits the telecommunications infrastructures that can be considered essential.[458] On the one hand, the duplication of the facilities has to be impossible or "extremely difficult owing to physical, geographical or legal constraints or is highly undesirable for reasons of public policy".[459] On the other hand, the facilities have to be vital for the development of the downstream competitor.

The traditional exclusive rights introduced a legal barrier to duplication that was eliminated by Directive 96/19/EC. Physical or geographical barriers do not seem to totally exclude competition from the most relevant telecommunications markets. Even if the scarcity of frequencies or rights of way for the installation of networks might limit competition, it cannot be held that it generally excludes it. The effect of the economic barriers, on the contrary, might prove more real. The already described economies of scale in the network industries, and also in the telecommunications industry, complicates market entry.

Reality is proving that economies of scale do not make the duplication of the incumbent's network impossible, as new infrastructures are being installed all over Europe.[460] All kinds of infrastructures are being duplicated, from dark

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[458] In this way, it seems rather clear that the Commission, after *Oscar Bronner*, would not make such a clear statement on the nature of a facility as essential as in *Atlas*: "However, even when all telecommunications facilities and services are non-reserved, FT and DT will at least for a number of years remain indispensable suppliers of building blocks for the relevant services in France and Germany [...] such facilities and services which remind an essential facility after full and effective liberalization [...]".

[459] *Ibid.* Opinion of the Advocate General, para. 64.

[460] The Commission bases its approach on the Access Notice on this fact, para. 53.

fiber to the local loop, so it cannot be sustained that duplication, in general, is not possible.

Even if most of telecommunications infrastructures are capable of duplication, or unless efficient substitutives can be developed,[461] and therefore, they should not be considered essential facilities by the ECJ, it is also clear that duplication of the development of substitutes will take a significant amount of time, and at least during such a period, the double monopoly will be unavoidable unless access is imposed on the monopolist.

A fundamental question therefore arises as to whether facilities that can be duplicated but not in a short period of time, are to be considered essential facilities. The Commission's Access Notice points in continuation the fact that building alternative infrastructures takes time, and as a consequence seems to adopt the position that during the transitional period, even facilities which are duplicable can be considered essential facilities. The judgement of the CFI in *Night European Services*, when analysing the vital character of certain facilities under the essential facilities doctrine, introduces a reference to "the time reasonably required for reproducing them" as one of the special characteristics which preclude the disponibility of alternative available for potential competitors.[462]

Nevertheless, Advocate General Jacobs in *Oscar Bronner*, when considering the very same practice of the Commission, points to the permanent character of the unavoidable monopoly, against its temporary character, as the main element to consider a facility essential.[463] Actually, the exceptional

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[461] This seems to be the assumption of the Commission, as it is continuously repeated in the Access Notice, for instance in para. 52.

[462] *Vide Night European Services* para 209 (*supra* footnote 430).

[463] The Advocate General even quotes Temple Lang, who pointed out that the test consists in checking "whether the handicap resulting from the denial of access is one that can reasonable be expected to make competitors' activities in the market in question either impossible or permanently, seriously and unavoidably uneconomic", in TEMPLE LANG, J. (1994): "Defining Legitimate Competition:

character of the essential facilities doctrine, derived from the unavoidable monopolisation of a vertically integrated market, does not seem compatible with the more relaxed view that would extend such an exceptional intervention to a market in which competition is developing. Moreover, the introduction of the compulsory granting of access would diminish the incentives for the investment in alternative infrastructures and obstruct the development of competition by the new comers.

In any case, it is possible to envisage the existence of specific infrastructures for which duplication is not viable. This is the case of the local loop in rural areas, where high costs and reduced traffic sometime excludes even the viability of a single network, and might be the case of other infrastructures which meet a very specific demand. In any event, the impossibility to duplicate the facility will have to be decided case by case, attending to the specific economic circumstances.

The second requirement, the facilities' character of "indispensable to carrying on that person's [the downstream operator] business",[464] is generally met in most of the cases of network access. It is clearly met in the case of service providers requesting network access for the provision of their services to consumers. It is also met by network operators requesting access for the completion of the communications initiated in their networks. In both cases, refusal of access to a network would definitely block their activity.

The refusal to grant access to such essential facilities necessarily excludes competition from the downstream markets, and as a conclusion, it seems to be the case that certain telecommunications infrastructures meet all the

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Companies' Duties to Supply Competitors, and Access to Essential Facilities", in "*Annual Proceedings of the Fordham Corporate Law Institute*", pp. 284-285.

[464] *Ibid.* para. 41.

requirements in order to apply the essential facilities doctrine for the compulsory provision of access to the facilities.

163. Access to essential telecommunications facilities. Despite the efforts of the Commission to limit the essential facilities doctrine to the exceptional cases in which no competition exists between the monopolistic provider of an essential facility and the new comers to a downstream market where the incumbent is not present, the essential facilities doctrine is to play a far more important role, particularly after the clarification of the doctrine by the ECJ.

Essential facility have been defined by the ECJ as the resource which objectively cannot be duplicated (and therefore is necessarily monopolised) and which is absolutely necessary for a downstream competitor for the development of its activity. This exceptional circumstance justifies the almost automatic abusive character of the refusal to grant access to essential facilities, as it will always have an exclusionary effect. Only allegations based on the potential harm for the monopolist could justify the refusal to deal, but never allegations based on efficiency, as potential benefits would never be passed to consumers due to the lack of even potential competition. It is not relevant whether competition exists or not in the vertically integrated market, whether access is required for the provision of a service already being provided by the monopolist or by a third company or whether it is required for the provision of a new service. The refusal to grant access to an essential facility will always have exclusionary effects.

However, imposing the obligation to grant access is only the point of departure, as the necessary consequence is that the lack of competition requires public authorities to regulate the conditions of such access. Obviously, the most

important access condition is price.[465] Different pricing practices are considered by the Access Notice as potentially anticompetitive. Excessive pricing, predatory pricing, price squeezes or discriminatory pricing are among them.

The frontier between proscribing an anticompetitive price, and regulating prices is easily passed, particularly under the regulatory tradition of Article 82 EC Treaty. Competition authorities can determine the anticompetitive character of a specific pricing policy, but cannot prescribe the pricing policy of a dominant operator, as it lacks the mechanisms of intervention for a continued control and the definition of comprehensive *ex ante* obligations. It is for this reason that competition authorities, in case competition is excluded, have to rely on the intervention of the regulatory authorities. It does not mean that competition authorities have no role to play. On the contrary, competition authorities can obstruct and fine anticompetitive behaviours when existing, and rely on the subsequent intervention of the regulatory authorities for the control prescription of a pro-competitive pricing policy.

In those cases in which the undertaking controlling the essential facility is vertically integrated, non-discrimination is the basic principle that should rule the pricing policy of the monopolist. As the principle ruling the essential facilities doctrine is to ensure that the control of an essential facility does not expand the monopoly power to a vertically related market, the simplest way to impede anticompetitive effects of the monopolist's pricing policy is to impose on it the obligation to provide the essential facilities at the same conditions enjoyed by the vertically integrated division. Comparisons nevertheless, are not always simple. Transparent cost accounting, with clear cost allocation principles and separation between different activities becomes a fundamental instrument for the analysis of pricing policies. Only a regulatory approach can

[465] See CAVE, CROWTHER and HANCHER (1995): "*Competition Aspects of Access Pricing*", European Commission, Luxembourg.

prescribe *ex ante* the implementation of such measures by the incumbent operators. Competition authorities thus, will often need to rely on the cost accounting principles defined by the regulatory authorities.

The Commission's Access Notice seems to imply that an access price clearly above costs is contrary to the rules on competition even if non-discriminatory as applied to the vertically integrated division of the monopolist. It seems difficult to identify exclusionary effects on such a pricing strategy. Nevertheless, such a policy might, however be considered unfair for the clients and therefore suppose an exploitative abuse. Advocate General Jacobs in *Sacem* sustained that in cases of absolute economic dependence, it would probably be an abuse to "charge what the market can bear".[466]

Even if the ECJ has recognised the unlawful character of excessive pricing and has even established parameters in order to determine when a price is excessive, it has never managed to identify a specific price as excessive. The reason might be that it entails a complicated and intrusive intervention which competition authorities cannot easily develop themselves. The coexistence of regulatory authorities with powers to determine prices might facilitate the intervention of the competition authorities, as stated in *Ahmed Saeed*.[467] Nevertheless, it has always to be taken into account that regulatory authorities consider a broader set of considerations when fixing prices, and as a result competition authorities cannot always rely on the prices fixed by them. For instance, it seems to be the case that competition authorities cannot rely on Long-run Average Incremental Costs accounting due to the uncertainties it entails as it focuses more on estimations of future costs than of historic costs.[468]

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[466] *Sace,* Cases C-110/88, 241/88 and 242/88, 1989 ECR 2811.

[467] *Ahmed Saeed,* Case 66/82, 1989 ECR 838, para. 43.

[468] See TEMPLE LANG, J. (1998): "Community Antitrust Law and national Regulatory Procedures", in "Fordham Corporate Law Institute", pp. 297-331.

Predatory pricing, despite the considerations in the Access Notice, does not seem a possible practice regarding essential facilities. Since the only facilities which are considered essential by the ECJ are those which cannot be duplicated, that is, those which are intrinsically monopolistic, it is in every case unnecessary for the monopolist which does not face even potential competition in such market to lower its prices to exclude a competitor from such market. It has to be considered, on the contrary, the possibility of a price squeeze through a combination of high prices for access to the essential facility and low prices for the provision of the vertically integrated service.

As regards non-economic conditions of access,[469] and particularly the point of interconnection, the Commission has adopted a very aggressive approach as the Access Notice states that "in principle, competition rules require that the party requesting access must be granted access at the most suitable for the requesting party, provided that this point is technically feasible for the access provider". The basic principle, however, should be once again that access has to ensure the possibility of effective competition in the vertically related market and therefore every discrimination between the vertically integrated monopolist and the downstream competitors has to be excluded. As a consequence, access should be provided at a point that allows the new comer to compete in equal terms, which is not necessarily any point he might require.

164. Access to non-essential telecommunications facilities. No general obligation to provide access to non-essential facilities exists. On the contrary, it has been sustained that such an obligation would not only be unworkable but would also be anti-competitive in the longer term.[470] Nevertheless, a dominant

[469] See WATERS, P. and WATTS, K. (1997): "Non-Price Terms of Interconnection", in *Computers and Telecommunication Law Review*, no. 2, pp. 61-65

[470] *Oscar Bronner*, para. 69.

undertaking's refusal to grant access can be considered abusive in certain occasions, particularly if linked to other conditions. This seems to be the case of cut off of supply to existing customers or the elimination of competition in a related market by tying separate goods or services. The structure of the European telecommunications markets fosters the development of these practices directed to exploit existing clients or to exclude new comers and potential competitors from the de-monopolised markets.

In any case, objective considerations could always legitimate the refusal to deal. Such justifications do not only comprise the situations in which a direct harm could be produced for the undertaking (i.e. credit risk) as in the essentials facilities doctrine. The effects on efficiency should also be considered, as long as the refusal would not exclude competition and therefore the pressure on the dominant firm to pass the benefits to the consumers. It has to be recognised, that this might be often the case in the telecommunications markets due to the lack of effective competition in most of the market segments due to decades of exclusive rights

As regards access conditions, it would seem that the rules on competition should not impose conditions as restrictive as in the case of essential facilities. Particularly, the automatic application of the non-discrimination rule should be excluded. Since competition, unless potential, is possible, it should be left for the dominant undertaking to freely contract with the operators requiring access. The application of the rules on competition should be restricted to exceptional exclusionary or exploitative practices. On the one hand, the rules against exploitative abuses would apply as regularly. As a consequence, excessive pricing could be considered exploitative but only in exceptional circumstances, and certainly should not lead competition authorities to fix prices exclusively connected with efficient costs. On the other hand, it seems clear that those conditions which would in practice entail the same exclusionary effects as the very same refusal should be proscribed. At the same time, practices such as

predatory pricing should be watched, in order to avoid the foreclosure of the very same infrastructures markets.

In any case, it seems clear that the rules on competition cannot be over-stretched in order to accelerate the emergence of competition. Compulsory access should not be imposed on the owners of facilities which duplication is possible even if complicated or time-consuming. On the contrary, compulsory access might have anticompetitive effects as it deters entry in such markets as both vertical integration by the new comers and the development of alternative infrastructures by independent operators would be obstructed. It is not for the competition authorities but for legislative or regulatory authorities to consider the need of further measures, due the exceptionality of the origin of the incumbents' market power, in order to accelerate the modification of the telecommunications market structure.

8.6. CONCLUSIONS.

165. Final. The rules on competition provide useful mechanisms for public intervention regarding network access but, at the same time, face important limitations. The most important limitations are derived from the very same purpose for which the rules were adopted. The rules on competition were not designed to immediately ensure the satisfaction of the consumers, but to protect such satisfaction indirectly, through the protection of the competition mechanisms that should lead to such satisfaction. Furthermore, the rules on competition were not designed to actively promote competition but rather to obstruct behaviours that would restrict existing or potential competition. Finally, the rules on competition were not adopted to prescribe the conditions in substitution of the competitive process.

From the analysis of the application of the Community rules on competition to network access conflicts, it can be derived that the figure of

refusal to deal as well as the essential facilities doctrine do not provide effective mechanisms for the immediate protection of the general interest. Article 82 EC Treaty cannot ensure universal access to the basic telecommunications networks and services at an affordable price to all the European citizens.

The rules on competition protect the competitive process that is supposed to promote efficiency. As a result, it is ensured the production of the optimum quantity of output as well as the reasonability of prices, as the competitive pressure promoted the reduction of costs and in parallel of prices. Nevertheless, the rules on competition do not ensure the availability of access to all citizens at an affordable price, as prices adapted to decreasing cost might not ensure affordability, and the provision of access in particular areas or to particular final users could not be profitable. Competition Law does not provide mechanisms to immediately intervene in order to ensure the satisfaction of the general interest as regards access. Therefore, the universality of access to telecommunications services and networks has to be ensured through different instruments of public intervention.

Nevertheless, the traditional approach to exploitative abuses of dominant position, and in particular excessive pricing, might prove useful to obstruct particular practices governing access. The rules on competition do not provide mechanisms to implement a pricing policy as regards access, but do provide mechanisms to intervene in particular situations against specific behaviours.

Even if the rules on competition were designed in order to ensure the efficiency of the competitive process, such rules face important limitations in markets in transition to competition. The rules on competition provide effective mechanisms to obstruct the refusals of access which entail exclusionary practices, but cannot, in principle, impose access in order to promote the creation of competition. Competition Law protects competition but was not designed to create it.

The transplant of the essential facilities doctrine from American antitrust provides an exception to the principle just stated that competition Law protects but does not create competition. In those exceptional cases in which competition is not viable in a particular market for physical, economic or legal reasons, and access to the products of service generated by such market is essential for the development of an activity in a vertically connected market, the rules on competition have been applied in order to impose access to the facility. This seems to be the case in some telecommunications network markets. Nevertheless, such an approach stretches dangerously the application of the rules on abuse of dominant position, as it scope is not to ensure the effectivity of the mechanisms of competition in such markets but to substitute the inexistant market constraints by legal constraints. Such an intervention does not seem fully compatible with the philosophy behind the rules on competition and certainly no effective mechanisms for such substitution are made available by the rules on competition.

CHAPTER 9

SECTOR SPECIFIC REGULATION ON NETWORK ACCESS

SUMMARY: 9.1. General principles. 9.2. Regulating access by other operators. 9.3. Regulating access by consumers. 9.4. Conclusions.

9.1. GENERAL PRINCIPLES.

166. The origins of the ONP policy. Community authorities were always conscious of the central role of network access in the process of the reform of the European telecommunications markets. Such a role, nevertheless, has evolved significantly as de-monopolisation has reached more and more segments of such markets.[471]

The proposal launched in the Green Book of 1987 to eliminate the exclusive rights on terminal equipment and value-added services raised the first

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[471] See ALABAU, A. (1998): "*La Unión Europea y su política de telecomunicaciones*", Airtel móvil, Madrid, pp. 135-190.

concerns regarding network access. It was feared that the incumbents' exclusive rights over the networks and their vertical integration in the liberalised markets would allow them to obstruct access to their networks and in this way exclude the emergence of competition in the de-monopolised markets. It seems clear that the Community rules on competition would have enforced access to the monopolised networks, but long and burdensome procedures would have been necessary.

An agreement between the Commission and the Council for the co-ordination of the adoption of a Commission liberalising Directive and a Council harmonising Directive was only reached on 7 December 1989.[472] As a result, the very same day the Commission adopted the liberalising Directive 90/388/EEC,[473] (the Services Directive) it was adopted the legislation devoted to rule access to the networks: Directive 90/387/EEC,[474] so-called the "Framework Directive".

The Framework Directive was based on two basic concepts. Firstly, "the conditions of open network provision must be consistent with certain principles".[475] Article 3(1) of the Directive established that access must be based on objective, transparent and non-discriminatory criteria. Secondly, "[the conditions] must not restrict access to networks and services except for reasons of general public interest, hereinafter referred to as 'essential requirements'".[476] The essential requirements were initially restricted by Article 3(2) to security

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[472] Press Release of the Council of 7 December 1989, 479/89. See MONTERO and BROKELMANN (1999): *"Telecomunicaciones y televisión. La nueva regulación en España"*, Tirant lo Blanch, Valencia, p. 77.

[473] Commission Directive 90/388/EEC, of 28 June 1990 on competition in the markets for telecommunications services, OJ L192/10, of 27.4.90.

[474] Council Directive 90/387/EEC, of 28 June 1990, on the establishment of the internal market for telecommunications services through the implementation of open network provision, OJ L 192/1, of 27.4.90.

[475] *Ibid.* p. 1.

[476] *Ibid.* p. 1.

of the network, network integrity, interoperability of services and protection of data. These concepts were developed by the ONP Committee and resulted in the adoption of a number of Directives[477] and Recommendations[478] ruling access to particular types of monopolised infrastructures and services, and the periodical publication of lists of standards.

The ONP framework was originally introduced to permanently regulate access conditions to legally monopolised facilities so that competition would be possible in the vertically connected services markets which had been de-monopolised. The legal monopolies permanently excluded the effectivity of the constraints introduced even by potential competition, so public intervention was required in order to ensure that the control of bottlenecks by the incumbents would not exclude the emergence of competition in the de-monopolised markets. The rules on competition could proscribe abusive refusals to grant access, but could not effectively prescribe access conditions. For this reason sector specific regulation was introduced.

167. ONP and the promotion of competition. The decisions to fully liberalise fully all the European telecommunications markets, including voice telephony and infrastructures required a major modification of the ONP policy[479] and legislation.[480] The elimination of the exclusive rights put an end to

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[477] Directive 92/44/EEC, of 5 June 1992, on the application of open network provision to leased lines, OJ L 165/27 of 19.6.92; and Directive 95/62/EC, of 13 December 1995, on the application of open network provision (ONP) to voice telephony, OJ L 321/6 of 30.12.95.

[478] Council Recommendation of 5 June 1992, on the harmonised provision of a minimum set of packet-switched data services (PSDS) in accordance with open network provision (ONP) principles, OJ L 200/1 of 18.7.92, Council Recommendation of 5 June 1992, on the provision of harmonised integrated services digital network (ISDN) access arrangements and a minimum of ISDN offerings in accordance with open network provision (ONP) principles, OJ L 200/10 of 18.7.92

[479] See COM(94) 513 final, Communication from the Commission to the Council and the European Parliament. Present Status and Future Approach for Open Access to Telecommunications Networks and Services (Open Network Provision), Brussels, 29.11.94.

[480] Directive 97/33/EC, of 30 June 1997, on interconnection in telecommunications regarding to ensuring universal service and interoperability through application of the principles of open network provision (ONP), OJ L 199/32 of 26.7.97; Directive 97/51/EC, of 6 October 1997, amending council directive 90/387/EEC and Council Directive 92/44/EEC for the purpose of adaptation to a competitive environment in telecommunications, OJ L 295/23 of 29.10.97; and Directive 98/10/EC. of 26 February

the barrier which excluded competition in the upstream markets, and therefore, put an end to the reason that, at least initially, justified pervasive access regulation.

In theory competition could be used in order to force the incumbents to provide access at reasonable conditions. Community authorities, nevertheless, considered that de-monopolisation would not automatically eliminate the market power enjoyed by the former monopolies. Potential competition was not considered enough to exclude abuses by the former monopolists, as effective constraints would only exist once alternative networks were be operative. As it was stated by the Commission "even when all telecommunications facilities and services are non-reserved, FT and DT will at least for a number of years remain indispensable suppliers of building blocks for the relevant services in France and Germany".[481]

The incumbents were in the position to abuse their market power. Abuses might have an exploitative nature, but also an exclusionary effect. Service providers could be excluded from the market and the development of network access services could be also hindered, as the development of alternative infrastructures heavily depends on the possibility to interconnect with the incumbent's network. Public intervention seemed necessary to ensure the emergence of effective competition as well as to avoid exploitation in the transitory period.

The rules on competition did not seem fully appropriate as they were not designed for the exceptional circumstances of transitional markets and for this reason would not always provide efficient solutions. The basic principles of the ONP, access at objective, transparent and non-discriminatory conditions,

1998, on the application of the open network provision to voice telephony and on universal service for telecommunications in a competitive environment, OJ L 101/24 of 1.4.98, which repealed Directive 95/62/EC.

seemed adaptable to the new situation, regarding both strictly network interconnection and access to the networks for the provision of services.

The adaptation required to take always into account that the instruments of permanent intervention under the ONP framework would play a subsidiary role after de-monopolisation. In case competition would exercise an effective pressure on the incumbent regarding the provision of network access, regulation would disappear.

However, the evolution of the traditional telephony market as well as the structure of new electronic communications markets such as mobile communications or digital television might challenge the transitory character of sector specific regulation on network access. Electronic communications markets, both the more traditional and the new markets, have a strong tendency to adopt a oligopololistic structure. The characteristics of network industries, already analysed, tend to reduce the number of operators in the market and to foster strategic behaviours which reduce competition. The rules on competition might not be sufficient to guarantee the effectiveness of competition so sector specific legislation might be necessary in the future.

168. ONP and the immediate protection of the general interest. Full liberalisation raised a different concern. The traditional market structure of the sector, the public national monopolies, allowed public authorities to develop a policy of cross-subsidiarisation between different market segments aimed at ensuring the universal availability of the basic telecommunications networks and services. Full liberalisation excluded such cross-subsidies in such a way that a different mechanism was required for the satisfaction of the general interest objective of the universal provision of the services.

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[481] *Atlas/Global One*, Commission Decision 96/546, OJ 1998 L 239/23, para. 34.

The rules on competition did not provide the necessary mechanisms to ensure universality.[482] Therefore, the regulatory mechanisms of indirect intervention were required. The ONP principles, introduced at the beginning of the process of reform of the European telecommunications markets, provided the necessary framework for the development of the policy of universal service. Universal service policies respond to different principles (immediate intervention, non structural) and different necessities (final consumers versus operators). In any case, access to telecommunications networks was the issue, and the principles of the ONP policy were fully compatible with the objectives and requirements of such a policy.

169. The leading assumptions. The application of the ONP framework after full liberalisation is based on two leading assumptions. The first one is that regulation is a subsidiary instrument introduced to eliminate market failures. The second one is that such intervention should always be characterised by its pro-competitive results. In other words, it should never obstruct the effectiveness of the mechanisms of competition which are supposed to govern the sector after liberalisation.

The basic scope of the process of reform of the European telecommunications sector is the substitution of the public leadership for the mechanisms of supply and demand in the market. It is assumed that private contracting between the operators, on the one hand, and between operators and consumers on the other, will be increasingly sufficient to ensure access at fair conditions. Public intervention should be limited to facilitate and promote private contracting, and pervasive regulation in substitution of the will of the actors in the market should be restricted to those exceptional cases in which it is the only mechanisms for ensuring the satisfaction of the general interest.

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[482] *Vide supra* Chapter 8. Competition Law and Network Access.

This assumption can be abstracted for a number of provisions in the ONP directives. The most clear example is the content of Article 5(1) of Directive 98/10/EC, which restricts the implementation of universal service schemes only "if necessary". Article 3 of Directive 97/33/EC according to which "Technical and commercial arrangements for interconnection shall be a matter for agreement between the parties involved, subject to the provisions of this Directive and the competition rules of the Treaty". The same reasoning informs the definition of conditions of access and use of public telephone networks, and leased lines.

The most important consequence of such a principle is the transitory character of an important share of the regulatory framework in the ONP directives. Community authorities opted for the adaptation of the old ONP framework in order to accelerate the development of alternative infrastructures and to ensure service providers access to the existing infrastructures.[483] Compulsory interconnection would ensure the developers of alternative infrastructures the benefits of the network externality effects, while compulsory access would ensure service providers the disposal of a network to reach consumers. The emergence of competition, nevertheless, is supposed to erode the incumbents' market power in such a way that fair trading conditions will be ensured by the very same constraints of competition rather than by public intervention.

On the contrary, it seems clear that in certain exceptional circumstances competition might not appear. Certain telecommunications markets do not offer the necessary profitability for private operators to provide network access. It might equally be the case that market conditions could exclude the presence of

[483] This was a political option subject to criticisms both by those who considered that market mechanisms should have played a more decisive role in the period of transition, and by those who consider transitory public intervention timid.

more than one network provider in a particular area. In such situations the ONP principles could acquire a permanent role in the telecommunications markets.

The other relevant assumption is that in any case, regulatory intervention as regards access should neither obstruct nor distort competition. Since competition is supposed to govern the sector after liberalisation, public intervention should not interfere in the competitive process, as other wise the constraints imposed by competition would be distorted and unable to ensure the satisfaction of the general interest. It is common in the harmonising directives, for this reason, to find references of the following kind: "national regulatory authorities shall ensure that such [interventions] do not result in distortion of competition".[484]

The basic principles of the ONP framework as defined in Article 3(1) of Directive 90/387/EEC but also in all the other directives on network access, seem useful in order to avoid distortions. They have to be based on objective criteria, defined in a transparent way and published, in such a way that they must guarantee equality of access and must be non-discriminatory.

170. Potential regulatory failures. Regulatory failures can be classified into two different categories. On the one hand, regulation can fail if it does not provide a solution for an existing problem. This would be the case of lack of intervention due to "regulatory capture", loopholes in the legislation etc. On the other hand, regulation can fail if it provides a solution for a problem which does not exist. This would be the case of the imposition of regulatory obligations regarding access to operators with no market power, or excessive obligations on operators which enjoy it. Over-regulation would also exist if unjustified regulatory obligations were to survive the transitory period and were to be applied after the emergence of effective competition in the market.

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[484] Article 7(3) Directive 97/33/EC.

The regulatory framework on network access might fail to provide an effective solution to an existing conflict for different reasons. It might be due to the well-studied phenomenon of the "regulatory capture". The regulatory authority might protect the interest of one of the regulated undertakings rather than the general interest in a particular access conflict as a result of the more effective pressure of that company. The regulatory authority in charge of determining the content of a specific obligation might not do so in an efficient period of time, or might impose non-reasonable conditions in favour of one of the parties involved in an access conflict. The lack of independence of some of the national regulatory authorities might in particular benefit their national champion. It might also be the case that the lack of an effective intervention had an objective reason such as the lack of the appropriate legislative basis. This might be particularly the case of access conflicts related to convergence, as national legislation might not foresee all the implications of this process.[485]

In case regulation fails to protect the rights of an undertaking in an access dispute, competition Law might prove useful to act as a safety network and might provide a solution to the conflict. The Commission, in the Access Notice, made clear its intention to intervene, upon request of the complainant, through the application of the Community rules on competition in case an NRA would not provide a solution within a six month period.[486]

More complex, but equally a potential regulatory failure, is the case of over-regulation. Such would be the case of the imposition of certain regulatory obligations regarding access to operators with no market power.[487] Such

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[485] UNGERER, H. (2000): "*The Case of Telecommunications in the E.U.*", in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gossling Ed., Hart, pp. 211-236.

[486] See Notice on the application of the competition rules to access agreements in the telecommunications sector. Framework, relevant markets and principles, OJ 1998 C 265/2, of 22.8.98 para. 30.

[487] As it is recognised by Directive 97/51/EC in paragraph 3: "in moving to a competitive market, there are certain obligations which should apply to all organisations providing telephone services over fixed

operators suffer not only the regular constraints of competition but furthermore the potential abuses of the former monopolists. Imposing regulatory obligations on these operators might create an unnecessary burden on the new comers which would obstruct the emergence of competition in the sector.

A similar situation would be the imposition of unproportionate obligations on operators which do have market power, but which, in any case, start to face competition from the new comers. A regulatory framework which imposes too heavy conditions on the incumbents could be anticompetitive as it might not promote efficiency among the new comers, which would be in grade to be profitable without beating the efficiency levels of the incumbent. Furthermore, such a situation could deter investments in particular segments for the development of alternatives to the new comer. Such a policy would have a similar effect than a predatory pricing strategy by the incumbent. It might ensure the monopolistic position of the incumbents in important market segments as the local-loop infrastructures.

The Community rules on competition might, once again, be used by the Commission in order to eliminate such anticompetitive intervention of the regulatory authorities. The Access Notice has made clear that the national regulatory authorities have a duty not to approve any practice or agreement contrary to Community competition Law and must ensure that action taken by them are consistent with Community competition Law.[488]

Finally, the maintenance of the access regulatory framework after the emergence of effective competition in the telecommunications markets would amount to over-regulation. Even if the Directive foresees the elimination of the regulatory obligations in such a case, it might easily be the case that the NRA

networks and [...] here are others which should apply only to organisations enjoying significant market power".

refuse to give up their regulatory powers regarding network access and continue to impose what then would clearly be unproportionate obligations on the operators. Such obligations would distort the markets, as they would impose a burden on certain categories of operators and would discourage investments and innovations.

9.2. REGULATING ACCESS BY OTHER OPERATORS.

9.2.1. General Considerations.

171. Introduction. Private contracting is recognised both by Community and national legislation as the basic mechanism ruling network access, particularly when access is negotiated between operators. However, negotiations for the conclusion of network access agreements face important barriers. On the one hand access is technically and economically complex. On the other hand, some operators might not have the necessary incentives to conclude such agreements as they strengthen the position of actual or potential competitors. For these reasons, regulation has been introduced in order to ensure access to the networks.

On the one hand, a set of regulatory obligations has been introduced in order to facilitate the conclusion of private agreements. Different mechanisms have been designed to reduce the burden of the technical and economic complexity of the agreements as well as asymmetry in the negotiations. These regulatory obligations do not intend to impose access or the conditions in which it should take place. On the contrary, they merely intend to promote the conclusion of private agreements, as it is understood that private contracting should be the regular mechanisms governing access in a liberalised market,

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[488] *Vide* Access Notice para. 13 and 19 (*supra* footnote 486). This point is further elaborated in Chapter 10.2.2. Antitrust Complements Regulation.

while regulatory intervention should be restricted to those cases in which an agreement defining fair access conditions cannot be reached.

On the other hand, regulatory mechanisms have also been developed in order to ensure that in case access agreements are not reached, public authorities can impose them. Such an intervention has a subsidiary character, as it only takes place once operators have been unable to reach an agreement despite the regulatory measures introduced to facilitate such agreements.

Compulsory access is complemented by regulatory mechanisms whose purpose it is to define access conditions, otherwise the mere obligation to provide access would be insufficient. Pricing as well as technical conditions of access might have to be defined by the public authorities. Such an aggressive intervention should always respect the basic ONP principles of proportionality, non-discrimination and transparency, in order to avoid over-regulation and the obstructions of the emergence of effective competition in the telecommunications markets.

9.2.2. Regulation Facilitating Private Agreements.

172. In general. The regulatory framework created by the Community authorities and implemented by the Member States contains a number of obligations aimed at facilitating the conclusion of private agreements governing network access, in particular network interconnection. The necessary inclusion of certain issues in the contract, the definition of deadlines in the negotiation and obligations about transparency as the communication of the agreements to the NRAs and the availability of such contracts to the competitors, the account separation and publicity and the existence of a Reference Interconnection Offer facilitate the negotiations. They allow for the overcoming the asymmetry of the bargaining power in the benefit of the weaker operators. Most of these obligations could be denominated mere formal

obligations, as they do not impose the conclusion of the contract nor any of the access conditions.

173. Basic content and deadlines. Article 9(2) of Directive 97/33/EC imposes on the Member States the obligation to promote the introduction in the interconnection agreements of the questions enumerated in part 2 of Annex VII of the Directive.[489] Member States have implemented such obligation which does not require them to impose the content of the agreements, but rather to determine the issues to be agreed by the operators. In this way, the negotiating power of the new comers is strengthened, as the incumbent cannot refuse to negotiate specific issues which are definitely relevant for interconnection. Nevertheless, the content imposed *ex ante* by the public authorities should be kept limited, as other wise the contracting freedom of the parties could be obstructed and market distortions could be introduced.

Another interesting mechanisms for the promotion of contracting is the definition of deadlines for the signing of the contract. Article 9(3) of Directive 97/33/EC allows NRA to define such deadlines at the request of a negotiating party or at their own initiative.[490] In Belgium, for instance, a six months term has been fixed and Belgacom's reference interconnection offer reduced such a term to five months, even if such term was often missed.[491] The parties can usually agree to extend the deadlines, but such extension cannot be imposed unilaterally. Once the deadline is over, any of the parties can claim the intervention of the regulatory authority. These deadlines strengthen the weakest

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[489] As regards particularly obligations related to content, see for instance Article 22(2) of the Spanish General Telecommunications Act implemented by Article 8(1) of the Regulation on Interconnection, Access and Numbering (RIAN), analysed in MONTERO and BROKELMANN (1999): "*Telecomunicaciones y televisión. La nueva regulación en* España", Tirant lo Blanch, Valencia, pp. 303-357; and VÁZQUEZ LÉPINETTE, T. (1999): "*La obligación de interconexión de redes de telecomunicaciones*", Tirant lo Blanch, Valencia.

[490] See PEREZ, R. (1999): "La negoziazione dell'interconnessione", in "*La disciplina giuridica delle telecommunicazioni*", Giuffre, Milano, pp. 169-179.

[491] In Spain, for instance, a four months deadline has been established for the completion of interconnection agreements and a deadline of three months has been established for access agreements. In Austria the deadline is of six weeks, and in Italy of 45 days.

negotiating party, as the menace of the NRA intervention avoids the introduction of unnecessary delays.

The lack of a similar provision in New Zealand forced CLEAR, the main new comer, to negotiate with the incumbent operator for four years before reaching a local network interconnection agreement. Even if forcing unnecessary delays in the negotiation could amount to an abuse of dominant position contrary to the rules on competition, a complicated and lengthy procedure would be necessary in order to obtain the declaration of illegality.

174. Transparency. Another set of regulatory obligations devoted to increase the success of private access negotiations tries to overcome the information asymmetry which benefits the incumbents both against the new competitors and even against the regulatory authorities. Specific obligations are imposed on the operators, and particularly on those with market power, in order to ensure that all the actors in the market have access to a sufficient amount of information. In this way, the benefits enjoyed by the former monopolists because of access to more information about the market and even about the competitors (through access agreements) can be distributed among all the actors. These obligations reduce the asymmetric negotiating position, as they allow new comers to increase their expertise as regards access agreements, even if they have never participated in such kind of negotiations.

Article 6 of Directive 97/33/EC imposes on Member States the obligation to ensure that operators with significant market power provide all the necessary information to those operators considering the possibility of requiring access to their networks. Furthermore, the existing interconnection agreements in which an operator with significant market power is involved should be made available to the new comers, excluding the commercial secrets but never the terms and conditions of interconnection nor the interconnection quotas. Article 16(9) of

directive 98/19/EC allows NRA to request details on the agreements for special network access.

It is interesting to note how some Member States such as Spain have expanded the reach of the Directives and have imposed such obligations not only on operators with significant market power but to all the operators in the market, even though the NRA could decide to exclude the agreements between operators which individually have a market share below 5%. In any case, operators only have access to the access agreements concluded by an operator with significant market power.[492]

Transparency is also promoted by the set of regulatory obligations imposed on operators as regards accounting.[493] Accounting separation is imposed by Article 8(2) of Directive 97/33/EEC on operators with significant market power which provide at the same time public telecommunications services and interconnection services. In these cases the operators are required to separate the accounting of the interconnection services (including those services provided internally) from the accounting of the rest of their services, in such a way that both costs and revenues of the interconnection services attributed according to defined criteria can be identified. Similar obligations are imposed by Article 18 Directive 98/10/EC regarding access to telephone networks and services. Accounting separation is also required by directives 97/33/EEC and 98/10/EC to those operators in the telecommunications services which enjoy special or exclusive rights in other sectors, such as electricity for instance.

The implementation of the relevant provisions by some Member States has, once more, expanded the obligations foreseen by the Directives from

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[492] Article 22(6) LGT and Article 2(7) RIAN. For the practice of the NRA on the issue *vide* MONTERO and BROKELMANN (1999), pp. 334-335 (*supra* footnote 489).

[493] See Arthur Andersen (1997): "*Accounting Separation in the Context of Open Network Provision*", European Commission, Brussels.

operators with significant market power to other operators active in the market. Such is the case of Finland, France, Luxembourg, the UK and Spain. In most cases, accounting separation applies to all operators with the exception of operators with a small turn over.[494] Such an expansion seems inconsistent with the explicitly recognised scope of the obligation, that is, to ensure non-discrimination in the provision of interconnection to third parties and to the vertically integrated division of the operator, and to make evident potential cross-subsidies. Both behaviours are forbidden to operators with significant market power but not to new comers without market power, so such formal obligations are unnecessary.[495]

Even the light-handed regulation introduced in New Zealand imposes obligations related to transparency[496] in order to over-come the information asymmetry between the incumbent and the rest of actors (including competitors but also public authorities).

175. Reference interconnection offer. Articles 3 and 4 of Directive 92/44/EEC as reformed by Directive 97/51/EC create the obligation for operators with significant market power in the leased lines markets to make public the technical and economic conditions of access to their facilities with an important level of detail. In such a way, operators requiring access can initiate negotiations for contracting access with a sufficient level of information.

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[494] Article 15(1) RIAN imposes such obligations on all operators with an annual turnover in the Spanish telecommunications markets of more than 3.340 millions of pesetas (around 20 million Euros).

[495] As a matter of fact, the Commission in Directive 97/51/EC para. 14 has recognised that "certain obligations concerning [...] cost accounting systems will no longer be appropriate once competition is introduced and [...] others can be relaxed by the competent national regulatory authority as soon as competition achieves the desired objectives".

[496] Telecommunications regulation of 1990, amended in 1993, imposes on the incumbent the obligation to disclosing accounting information, interconnection agreements and standard contracts. See WEBB and LATTERY (1999): "New Zealand", in *International Telecommunications Law*, pp. 23-24, BNA, London.

Article 7(3) of Directive 97/33/EC elaborated on this basis and reinforced the intervention in interconnection negotiations. A reference interconnection offer which includes a description of the unbundled elements of the network and the terms and conditions of interconnection has to be published by the operators with significant market power in the fixed telephony network and service markets as well as in the leased lines markets.

Even if Directive 97/33/EC allows NRA the power to impose modifications in the RIO when justified, it is not explicitly stated that NRA have to approve the RIO proposed by the operators with significant market power. Nevertheless, directly or indirectly, this is the way it works in most of the Member States.[497] As a result, the standard terms and conditions of interconnection are negotiated between the dominant operators and the public authorities, in a framework significantly more balanced than the existing in the market. It is for this reason that RIOs became one of the most conflictive elements in the process of reform of the sector. The Commission was forced to initiate infringement procedures against a significant amount of Member States for delays in the publication of RIOs by the former monopolies. Furthermore, the former monopolists have often challenged the modifications of their RIOs by the NRA before the Courts.

RIOs strongly facilitate interconnection. The RIO provides a precise description of all the facilities provided by the operator with significant market power as well as the minimum terms and conditions which are in any case enforceable on the operator. New comers disfavoured by the bargaining asymmetry have at their disposal all the relevant information they need, so they do not have to negotiate to get it. At the same time, the RIO provides a "floor" for the conditions of interconnection, as new comers can always improve the conditions in the RIO, but in any case the conditions contained there are

[497] This is clearly the case of Belgium, France or Spain or Italy.

assured to them. It is interesting to note that such a framework does not exclude the definition of a different structure by the operators.

176. Evaluation. These formal obligations introduce transparency in the market and reduce the asymmetry in the bargaining power in the negotiations for the conclusion of access agreements. It is obvious that most of the obligations suppose a burden on the operator which suffers them. Nevertheless, such a burden rarely limits the competitive ability of the operators with significant market power, as the financial burden is certainly reduced in relation to their turn over. At the same time, as long as they do not impose the specific conditions at which access is to be granted, they do not distort directly the market.

The extension of the formal obligations to operators without significant market power, as it has been done in a number of Member States, raises a series of questions. In the first place, it is necessary to evaluate the appropriateness of such an extension. In general, it is difficult to justify the imposition of these obligations to operators without market power. The lack of such power makes any abuse impossible. As new comers do not enjoy the control over an extensive network, it seems unnecessary to introduce formal obligations directed to ensure that such power is not used to obstruct the entrance to the markets of new operators.

Nevertheless, there are cases in which such an extension might be justified. The Community framework limits the application of most of these formal obligations to operators dominant in the basic fixed telephony markets, both network and service markets. In those markets where it is considered that enough competition exists, these obligations are not applied. This is the case of mobile telephony. As the mobile telephony markets are supposed to be competitive, the Community regulatory framework has excluded the application of most of the formal obligations to these operators, despite the fact

their reduced number allows the existence of market failures which might reduce the effective competition in the market. The Community framework, implemented by the Member States, allows for the extension of most of these obligations to the mobile operators exclusively if they enjoy significant market power in the national interconnection market.[498]

The extension of some of the formal obligations, and particularly of those directed to increase the transparency in the market, to the operators with significant market power in the mobile markets would allow NRAs to control the evolution of the markets and the significance of the market failures. At the same time, such extension would not directly distort the market, as the formal obligations do not entail the imposition of particular access conditions on the operators.

Finally, one has to consider the effect of the extension of the formal obligations to small new comers to the basic fixed telephony markets, as has been done in some Member States. Even if the burden imposed on operators with significant market power does not limit its competitive ability, it might be the case that the imposition of some of the obligations to very small operators could suppose a decisive burden to their small administrative resources. As a result, a rule excluding very small operators from the obligations should be in any case considered.

9.2.3. Compulsory Access.

177. Compulsory access. The ONP framework, even after full liberalisation, is based on the assumption that major market failures can be identified in the European telecommunications sector. The existing ONP

[498] NRAs have been reluctant to declare mobile operators as SMP holders. This was particularly the case for mobile operators with a market share under 25%. Despite the pressure by fixed operators to have them declared as SMP operators due to the important distortions found in the mobile market, NRAs were reluctant to intervene due to political pressure, the legal uncertainty and even the lack of faith in the SMP scheme, as the very same Commission proposed to modify it in November 1999, when the declaration was to take place in many Member States.

framework pays particular attention to the market failures that seem to derive from the market power inherited by the incumbents after decades of monopolisation.

All the relevant directives contain explicit provisions which impose on incumbent operators the obligation to grant access to their networks or services. Particularly clear is Directive 97/33/EC regarding interconnection: "Organisations authorised to provide public telecommunications networks and publicly available telecommunications services [...] which have significant market power shall meet all reasonable requests for access to the network including access at points other than the network termination points offered to the majority of end-users".[499]

The Community Directives have always paid particular attention to the objective justifications which could legitimise the refusal to grant access to the networks. A closed list of the so called essential requirements which would legitimise the refusal has been developed by the Community authorities. The list of essential requirements comprises justifications based on the security of network operations (in order to ensure the availability of the services even in cases of *force majeure*), on the maintenance of network integrity, on interoperability of services, on protection of data and on the effective use of frequency spectrum.[500] Community legislation excludes any objective reason based on the efficiency derived from the refusal to grant access.

178. Transitory character. The generalised application to the incumbents of the ONP framework after the full liberalisation of the sector can

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[499] This is the case of Article 3 Directive 90/387/EEC, as amended by Directive 97/51/EC; Article 6 of Directive 92/44/EEC as amended by Directive 97/51/EC; Articles 13 and 16 of Directive 98/10/EC.

[500] See Article 3(2) of Directive 90/387/EEC as amended by Directive 97/51/EC, Article 6 of Directive 94/44/EEC as amended by Directive 97/51/EC, Article 10 of Directive 97/33/EC, and Article 13 of Directive 98/10/EC.

only be understood as an exceptional policy for the period of transition, in order to accelerate the emergence of effective competition in the sector.

As a matter of fact, the ONP Directives contain numerous references regarding the reconsideration of the application of the ONP principles in markets where effective competition exists. For instance, recital 15 of directive 97/51/EC states: "it is appropriate to allow the requirements for cost orientation and transparency in specific markets to be set aside where [...] effective competition ensures that tariffs for leased lines are reasonable". In the same line, recital 14 of Directive 98/10/EC goes further and states that the compulsory access and ONP principles "will no longer be appropriate once competition is introduced".

The transitory character of the ONP regime is implicitly recognised by the introduction of a process of review of the ONP directives whose beginning was fixed for 31 December 1999. The review was suppose to examine "the removal of obligation no longer needed in a market where there is effective competition".[501]

179. Access conditions. The open network provision policy not only imposes access to the networks, but also tries to harmonised access condition in the European Union. The basic principles were already defined in Article 3(1) of Directive 90/387/EEC. Network access should always be based on objective criteria, be transparent and published, and guarantee equality of access and non-discrimination. These principles have always informed the harmonisation of the access conditions by the Directives which have developed the ONP framework. Particularly interesting has been the application of the non-discrimination principle, as it has required vertically integrated incumbents to

[501] Recital 17 of Directive 98/10/EC. Similar considerations can be found in Article 14 of Directive 92/44/EEC as amended by directive 97/51/EC: and recital 25 of Directive 97/33/EC.

grant third parties access to their facilities at the same conditions at which their vertically integrated divisions or partners have access.[502]

Full liberalisation has forced the modification of the conditions for the application of the ONP framework. However, such a relevant reform of the sector has not significantly modified the fundamental principles of the ONP policy, particularly the non-discrimination principle. The reason seems to be that the elimination of the exclusive rights does not automatically eliminate market power, and that the control over the only existing universal network by an incumbent can distort competition in the period of transition to effective competition.

180. Access pricing. Tariff principles were always considered among the access conditions which required harmonisation in order to "ensure fair and transparent conditions for all users".[503] Tariffs should then be based on objective principles, be transparent and non-discriminatory. These general principles determined the basic rule which has governed access pricing in the ONP framework: prices should be cost oriented.

The lack of competition in the access market due to the exclusive rights over infrastructures and the telephony service excluded supply and demand mechanisms for the definition of access prices. Price determination could not be left to the monopolist, as they could try to exclude new comers to the services market and to obtain monopoly rents. It was necessary to harmonise at a Community level the basic principles ruling access pricing. Objectivity, transparency and non-discrimination were the general principles defined for access conditions. Efficiency was another important requirement, as well as the financial stability of the monopolists. Cost orientation provided a valid mechanism in order to meet all these requirements. "Cost orientation implies

[502] Article 6 of Directive 97/33/EC; and Article 16(7) of Directive 98/10/EC

that the price charged for provision of a service should reflect the underlying cost incurred in providing that service".[504] Annex II of Directive 90/387/EEC established the basic lines for price regulation by the national authorities.

Cost orientation was supposed to introduce not only objectivity but also fairness and efficiency in access pricing. Since exclusive rights excluded competition as the force defining prices, it was for public authorities to determine access pricing, in a way which would substitute as closely as possible market pressures. Directive 92/44/EEC was the first one to introduce cost oriented pricing in the European telecommunications markets. Article 10 not only determined that prices should be cost oriented but also transparent, and in order to ensure this, introduced the obligation to develop cost accounting systems suitable to ensure the effectivity of the pricing policy. Community authorities were fully aware of the difficulties of determining prices in the telecommunications industry, and for this reason, determined some basic principles for cost allocation according to the direct or indirect relation between costs and a particular service. Nevertheless, at that initial point no guideline was developed as regards the criteria for cost analysis.

Full liberalisation has not eliminated the principles of non-discrimination and cost oriented pricing, even if such principles have been restricted to access to certain facilities of operators with significant market power. Article 17 of Directive 98/10/EC confirms the application of the principles defined in Annex II of Directive 90/387/EEC, as amended by directive 97/51/EC, to access to telephony networks and services. The same principles apply to interconnection to networks of operators with significant market power according to Article 7(2) of Directive 97/33/EC, which explicitly imposes on such operators the burden to prove that their access prices are determined by their real costs.

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[503] Directive 90/387/EEC, p. 1.

[504] See Commission Recommendation 98/195/EC of 3 January 1998, on interconnection in a liberalised telecommunications market (Part 1 –Interconnection pricing), OJ L 73/42 of 12.3.98.

181. Cost analysis. Cost accounting, nevertheless, is not a very precise science. Different costing methodologies coexist in the market in order to give responses to different situations and also to different interests.[505] The adoption of the accounting methodology was left for the national authorities, even if the Commission has expressed its preference for the application as regards interconnection of the Forward Looking Long Run Average Incremental Cost approach, both in the Directives[506] and in specific Recommendation on the subject.[507]

Fully Distributed Historic Costs, the traditional accounting methodology of the national monopolists, lacks the required objectivity, as the distribution of costs is rather random. At the same time, historic costs do not seem compatible with a competitive environment where the firms price their assets according to their value in the market rather than according to the investment they undertook to develop the asset. This methodology determines very high access costs and does not promote increases in the efficiency of the dominant operator.[508]

Methodologies exclusively based on Marginal Costs, even if they better reflect the logic of competitive markets, do not seem the most appropriate for network industries, as they ignore the common and joint costs which are the

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[505] See BAUMOL, W. (1970): "Optimal Departures from Marginal Cost pricing", in *American Economic Review*, vol. 60, p. 265; CAVE, CROWTHER and HANCHER (1995): "*Competition Aspects of Access Pricing*", European Commission, Brussels; KAHN, A. (1993): "*The Economics of Regulation: Principles and Institutions*" MIT, Cambridge MA; LAHN and SHEW (1987): "Current Issues in Telecommunications Regulation: Pricing", in *Yale Journal on Regulation*, vol. 4, no. 2, pp. 191-256; MITCHEL and VOGELSANG (1991): "*Telecommunications pricing: Theory and practice*", Cambridge University Press, Cambridge.

[506] See recital 10 of Directive 97/33/EC which states that "the level of charges [...] should not be below a limit calculated by the use of long-run incremental cost and cost allocation and attribution methods based on actual cost causation, nor above a limit set by the stand-alone cost of providing the interconnection in question; whereas charges for interconnection based on a price level closely linked to the long-run incremental cost for providing access to interconnection are appropriate for encouraging the rapid development of an open and competitive market".

[507] *Vide* Commission Recommendation 98/195/EC (*supra* footnote 504); amended by Commission Recommendation 98/511/EC of 29 July 1998, OJ L 228/30 of 15.8.98.

[508] See BRAEUTIGAM, R. (1980): "An Analysis of Fully Distributed Cost Pricing in Regulated Industries", in *Bell journal of Economics*, vol. 11, no. 1, pp. 182-196.

most relevant in industries such as the telecommunications, and therefore determine very low interconnection prices, which deter investments in alternative infrastructures. [509]

Forward Looking Long Run Average Incremental Costs avoids the pitfalls of the latest methodologies. On the one hand, this methodology focuses on the costs of the provision of extra units of a service, rather than on the historic investments of an operator. On the other hand, the consideration of the long run allows one to take into consideration not only the variable costs but also the fixed costs, which in the long run also become variable as they can be adapted to the supply.

The latest methodology even if theoretically sound, is not simple to apply in practice and introduces a high degree of uncertainty, as many of the parameters under consideration are mere estimations of the future development of the market. In any case, the definition by the NRA of the basic methodological assumptions introduced certainty and ensures the objectivity as well as the fairness of the system.[510] In any case, the implementation of such accounting systems by the operators with significant market power requires a considerable period of time (around 24 months), and for this reason the Commission has recommended the transitional adoption of a benchmarking approach.

Any cost accounting methodology requires a reliable cost accounting by the operators. In particular, cost accounting has to be transparent and allow regulatory authorities as well as competitors to confirm that the dominant operator's prices are related to objectively defined costs.[511] This can only be

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[509] See for instance BOS, D. (1994): "*Pricing and price Regulation. An Economic Theory for Public Enterprises and Public utilities*", Elsevier, Amsterdam, pp. 119-129.

[510] See ERGAS, H. (2000): "*TSLRIC, TELRIC, and other Forms of Forward looking Cost Models in Telecommunications: A Cunungeons Guide*", in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gossling Ed., Hart, pp. 105-130.

[511] *Vide* Arthur Andersen (*supra* footnote 493).

ensured if the distribution of common costs is objectively developed following the criteria defined by the regulatory authorities and if cross-subsidies inside the dominant operator are excluded.

182. Technical conditions. The principles of objectivity, transparency and non-discrimination govern not only the economic but also the technical conditions at which access is provided. Regulatory authorities not only have competencies to adopt standards in order to ensure interoperability and transparent access conditions, but already in Directive 90/387/EEC it was pointed out that other conditions such as quality of service, provision time (delivery period), fair distribution of capacity in case of scarcity, repair time, availability of network information and customer proprietary information, were to be harmonised. The ONP directives contain a substantial number of references to such conditions.

The most relevant technical condition, however, has been the unbundling of the networks. Directive 90/387/EEC already required to leave for users a choice between the individual service elements.[512] All the ONP directives contain references to these basic principle in order to ensure that "the applicant is not required to pay for anything not strictly related to the service requested".[513] Nevertheless, Community directives do not specify up to what level the incumbents' networks have to be unbundled. As a consequence one of the most important debates, the one on the unbundling of the local loop, was initially left for the national authorities. Member States were divided on this debate,[514] so finally the Commission had to intervene.

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[512] See Annex II of Directive 90/387/EEC.

[513] Article 7(4) of directive 97/33/EC.

[514] See a table with the different option in LEWIN, D. and MATHEWS, J. (1998): "Access Networks and Regulatory Meassures", OVUM for DG XIII, European Commission, Luxembourg, p. 60.

Local loop access at prices related to cost might allow new comers to benefit from the economies of scale enjoyed by the incumbent and would lower the risk for entering the access network market, which would accelerate local competition. On the contrary, it removes incentives for building alternative networks, complicates the modernisation of the incumbent's network and requires significant regulatory intervention.

183. Interconnection discrimination. Despite the fact the most established principle governing network access is non-discrimination, pressure by some Member States forced the introduction in Directive 97/33/EC of the following statement "different tariffs, terms and conditions for interconnection may be set for different categories of organisations which are authorised to provide networks and services, where such differences can be objectively justified on the basis of [...] the relevant national licensing conditions".[515]

Directive 97/33/EC states that "National regulatory authorities shall ensure that such differences do not result in distortion of competition". The potential effects on competition have been considered by the Commission in its Recommendation on interconnection pricing,[516] as well as in the Access Notice.[517] In the latest document the Commission considers that such a discrimination could never be the result of the application of Article 82 EC Treaty, and furthermore, analysis in the specific case could lead to the consideration of such an action as anticompetitive.

184. Enforcement. The ONP framework not only has established the basic lines governing access, based on the principles of objectivity, transparency and non-discrimination, but has also created a set of regulatory mechanisms to ensure the effectivity of such principles. Even if private

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[515] Article 7(3) Directive 97/33/EC.

[516] *Vide* Recommendation on interconnection pricing, point 5.1 (*supra* footnote 504).

[517] *Vide* Access Notice para. 123-125 (*supra* footnote 486).

negotiations are to determine initially the access conditions, a set of generic obligations are imposed *ex ante* on operators with significant market power. Furthermore, *ex post* mechanisms allow public authorities to intervene in case negotiations do not provide fair access terms and conditions.

On the one hand, a set of mechanisms can be identified by their conflict resolution nature. Regulatory authorities intervene to determine the conditions which cannot be agreed by private parties. On the other hand, mechanisms have been developed in order to impose fairness and avoid anticompetitive effects despite the lack of apparent conflict between he parties.

185. Conflict resolution. All the ONP Directives foresee procedures under the national regulatory authorities for the cases in which no agreement can be reached between the operators negotiating an access agreement. As it is stated in Article 16(4) of Directive 98/10/EC "National regulatory authorities shall [intervene] if requested by either party in order to set conditions which are non-discriminatory, fair and reasonable for both parties and offer the greatest benefit to all users".

Particularly detailed is Directive 97/33/EC on interconnection, as not only can operators require the intervention of the NRA, but the NRA is forced to provide a solution for the conflict in a six months period after the request of one of the parties. Furthermore, the NRA has the obligation to publish the motivated decision.[518]

Member States have implemented such obligations and as a result specific procedures for conflict resolution on access and interconnection are at the disposal of the operators for the fast and efficient solution of their conflicts.

[518] Article 9(2)(5) and (6) of Directive 97/33/EC.

186. Own-motion intervention. The ONP Directives do not only foresee the intervention of the NRA at the request of the operators. Intervention at the NRA motion is also envisaged by the Community directives.

Firstly, national regulatory authorities can intervene in order to ensure that access agreements include conditions which respect the principles of objectivity, transparency and non-discrimination, and that such agreements are implemented in an efficient and timely manner. Secondly, national regulatory authorities may intervene at their own initiative at any time where justified in order to ensure affective competition and/or interoperability.[519] In the case of interconnection agreements, the possibility for the NRA to impose the modification of a concluded agreement if it is justified in order to ensure effective competition or interoperability is foreseen.[520]

Finally, Article 9(6) of Directive 97/33/EC foresees that "in cases where organisations which are authorised to provide public telecommunications networks and/or publicly available telecommunications services have not interconnected their facilities, national regulatory authorities, in compliance with the principle of proportionality and in the interest of users, shall be able, as a last resort, to require the organisations concerned to interconnect their facilities in order to protect essential public interests and, where appropriate, shall be able to set terms of interconnection".

9.2.4. Evaluation.

187. ONP and essential facilities. The ONP framework was designed mostly to erode the market power of the incumbents derived from the control of the traditional fixed telephony network. In this way, new comers would have a chance to enter the market and compete with the incumbent. It is interesting

[519] See Article 16(4) and (5) Directive 98/10/EC.

[520] See Article 9(3) of Directive 97/33/EC.

to note that the ONP principles were built by the Commission on the principles ruling the essential facilities doctrine as understood by the Commission.

Firstly, obligations were imposed mainly on the incumbents due to their market power. Secondly, non-discrimination was in both cases the leading principle governing network access. Non-discrimination together with objectivity, transparency and proportionality were to ensure that the control of an asset by the former monopolies did not exclude new competitors from vertically connected markets, so that competition in equal terms between the incumbents and the new comers would be possible.

However the most relevant point is that the full liberalisation of the telecommunications markets modified the application of the essential facilities doctrine, but did not substantially affect the ONP framework. The application of competition Law, and in particular of the figure of refusals to deal and the essential facilities doctrine after the *Oscar Bronner* judgement, is determined by the market structure. Compulsory access is not automatically imposed by the rules on competition anymore in those markets in which duplication of the facility, and therefore some competition, is viable.

The ONP framework as it is designed nowadays, on the contrary, ignores the differences in market structure which clearly appear in the European telecommunications markets. No differentiation has been introduced in order to distinguish the regulation of markets which can be governed by competition and those where competition will necessarily be limited as a result of the existence of a market failure. The ONP directives maintain the obligation on the incumbents to provide access at non-discriminatory conditions, no matter

ehether actual or potential competition exists for the provision of a particular access.[521]

The lack of attention to market structure in the actual regime presupposes the application of the same regulatory intervention in very different situations. On the one hand, network access regulation tries to overcome the obstacle to the emergence of effective competition caused by decades of monopolisation and the presence in the markets of the traditional monopolists with all their market power. On the other hand, network access regulation imposes a market substitutive regime for those markets (very limited, but existing) in which effective competition is not possible as a result of the market structure (natural monopoly, low demand, inadequate technology etc.).

At the same time, the rigidity of the ONP framework, focused on a limited number of electronic communications networks markets (mostly fixed telephony networks and leased lines), prevents public intervention in new markets were market failures might be developing. This might be the case of mobile communications and digital television networks.

188. Transitory period. Regulatory intervention on network access has been confused by the contradictory mixture of objectives. It was usually considered necessary to foster the development of service competition by reducing obstacles to access including prices. At the same time, it was usually argued that very aggressive policies for access would deter investments in network development by new comers and as a result would obstruct network competition.

[521] DGXIII of the European Commission published a document on 21 May 1999 "DGXIII Discussion document on the 1999 Review: regulatory principles", in which it was recognised that the regulatory framework serves two purposes. Firstly, the setting out of measures to liberalise a former monopoly sector. Secondly, providing a harmonised framework for national legislation to ensure that the liberalised marketplace functions effectively. (See page 5).

Nevertheless, it seems clear that in case network competition would be discarded in some network markets, price regulation would have been different, as the elements to balance would have been the promotion of service competition on the one hand, and the mere financial equilibrium and efficiency promotion for the network monopolist on the other. As a result, more aggressive policies could have been implemented directly to foster access to necessarily monopolised networks by new comers to services markets. These considerations should have led price regulation for those network markets where competition was not feasible, but the inclusion of all network markets in the same debate has excluded a particular policy for non-competitive market segments.

The mixture of both objectives in the determination of access conditions and prices has introduced significant confusion. As NRAs have been forced to fix a unique access price independently of the market structure, their perspective on the possibilities for the emergence of effective competition in a smaller or larger portion of the network markets has influenced their network access policies.

In some countries where confidence in the emergence of effective competition has been reduced, an interventionist policy aimed at ensuring (somehow artificially) the attractiveness for new comers of the network markets has been pursued. This is a very distorted policy, as it fosters (and often it imposes) investments which might not be economically justified but are merely based on a distortion which does not foster efficiency and does not benefit consumers. Such a policy does not effectively foster network competition, as new comers are aware of the risks of this policy in the long-run and do not invest, and it certainly obstructs the emergence of competition in the service markets, due to the restriction to access, to the benefit of the incumbent.

An open acceptance of the limitations of the liberalisation process, and the instauration of a double policy according to market structures, would have avoided the divergent and often distortive policies on network access which have been identified in the Member States based on the different faith on the process. In any case, the actual system has to be complemented with explicit and enforceable mechanisms devoted to ensure that as soon as a market reaches an acceptable degree of competition, the regulatory intervention has to be eliminated.

189. Mature markets. The imposition of a common regulatory regime on network access despite the structure of the network market would increase its distortive character as competition emerges on those markets where it is feasible. As competition emerges, the criterion which should rule public intervention on the market should not merely be the market share of an operator, even the incumbent, and in particular the inclusion in the category of operator with significant market power. On the contrary, the criteria should be the feasibility of the emergence of effective competition in the market.

The permanence over time of operators with important market shares could be the result of the competitive process which recognised the most efficient provision of the service, or the result of a market failure which obstructs the effective constraints of competition. In the first case, it is for the rules on competition to obstruct abuses of such a dominance. In case there is a market failure, it is for regulation to govern the provision of the service by the dominant operator.

The extension over time of the framework designed to foster the emergence of competition would distort competition in those markets where it will emerge, as it would allow weak operators to survive as a result of the benefits introduced by the regulator. Such a situation would not benefit consumers, as efficiency would not be rewarded and income would be transferred from the users to the inefficient operators.

Over time, regulation on access should be limited to network markets with some kind of market failure. It could be argued that market share is the simplest mechanism to ascertain the lack of competition and therefore the existence of a market failure. Even if it is true that market share is a significant tool for the evaluation of a market, the application of the rules on competition has shown that many other factors have to be evaluated in order to determine the characteristics of a market. Moreover, a 25% market share is extremely low in order to ascertain the existence of a market failure.

A mere market share of 25% might justify the inclusion of an operator in the category of operators with significant market power. Nevertheless, it might easily be the case that an operator and particularly the incumbent, could have a 25% share in a network market, and a very reduced market power, due to the existence of a significant number of competitors, some of them with a similar market share, and vigorous competition in the market.

As a consequence, it seems that inclusion in the category of operators with significant market share should not be the leading criterion for the imposition of the regulatory obligations on access in the future. On the contrary, the evaluation of the characteristics of a market and the identification of a market failure should be the main criterion.

190. New markets. At the same time, the liberalisation regulatory framework was focused on the control of incumbents regarding the most traditional telecommunications markets: voice telephony services and infrastructures. However, recent years have witnessed the development of new network and services, particularly mobile communications and digital television. The regulatory framework paid very little attention to the first and none to the second.

The basic assumption was that since no exclusive rights existed in these markets, there was no need for a major intervention regarding access to these networks.

Nevertheless, the evolution of these market has proven that the oligopolistic tendency of network industries, reinforced by the distorsive effects of frequency scarcity, might produce important market failures which could require a regulatory intervention.[522]

Such intervention cannot be based on simplistic features like the market share or the number of operators active on the market. On the contrary, it is necessary to undertake a solid market analysis in order to evaluate whether market players suffer sufficient pressure in order to fulfil consumer demands.

191. Difficulties. It is clear that certainty has to be introduced in the evaluation of the structure of the market before deciding to apply the regulatory framework on network access. Such a decision is subject to pressure from the operators, and important risks of capture by the incumbent as well as by the new comers obviously exist.

This difficulty can be overcome by the participation of different institutions in the adoption of the decision. European institutions could draw the basic picture and define wide limits for the inclusion of certain markets in the regulatory framework. Such limits would be the object of periodical review in order to adapt the legislation to technical and economic evolution.

192. The 99 Review. As a matter of fact, as a result of the Review of the telecommunications legal framework, the Commission has proposed major reforms in the ONP regime.

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[522] See MONTERO, J. J. (2000): "*Competencia en las comunicaciones moviles. De la telefonia a Internet*", Tirant lo Blanch, Valencia.

The Directive proposal[523] introduces a deep reform in the access and interconnection regime. Firstly, the proposal is more flexible than the regime in force nowadays. It does not impose obligations on specific categories of operators based on an implicit identification of a market failure. On the contrary, it merely provides the mechanisms and procedures to identify market failures and provides instruments to solve such failures.

The new directive would not be centred in the regulation of access and interconnection to specific networks owned by specific categories of operators. On the contrary, it is applicable to all electronic communications networks, those existing at the moment (mobile communications, internet, digital television etc.), and which might develop in the future. It would even reach very specific network elements (set-top boxes, APIs etc.) in case it can be demonstrated that a market failure exists.

The intervention of the NRAs is not based on the prior identification in the Directive of a market failure. On the contrary, a flexible procedure for the identification of market failures is proposed. The Commission will publish regularly a list of markets in which market failures might exist, It will then be compulsory for the NRAs to analyse such markets (in collaboration with all market actors) in order to conclude whether a market failure can be identified in the national market. Any attempt to analyse markets outside of the list proposed by the Commission would have to be approved by the Commission.

A major reform proposed by the Commission affects the Relevant Market Power category. The Commission intended to maintain the category as it is, but many operators sustained that a 25% market share was too low for the NRAs to intervene. The Commission has finally proposed to consider an operator as

[523] COM(2000) 384, "*Proposal for a directive of the European Parliament and of the Council on access to, and interconnection of, electronic communications networks and associated facilities*", Brussels, 12.7.2000.

having Significant Market Power if " either individually or jointly with others, it enjoys a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, consumers and ultimately consumers".[524]

This reform is of major importance. It seems that the Commission proposes to limit the application of the regulatory framework to those operators which can be considered as dominant according to the rules on competition. At the same time, it seems to shift the focus from individual dominance to collective dominance, as many telecommunications markets are adopting an oligopolisitic structure.

Finally, the Commission proposes a closed list of obligations which might be imposed on operators with significant market power in markets with a failure. These obligations are basically the same as in the regime in force nowadays. It is for the NRAs to decide which obligations are necessary in order to overcome the failure. In case an NRA intends to impose a different obligation, it needs the approval of the Commission.

The new regulatory framework recognises the need for a more flexible approach based not in the mere existence of a high market share, but on the identification of a market failure. Even further, the new regime recognises that such failure will not be caused only by the market strength of the incumbents, but also by the oligopolistic structure of the electronic communications markets.

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[524] See COM(2000) 393, , "*Proposal for a directive of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services*", Brussels, 12.7.2000.

9.3. REGULATING ACCESS BY CONSUMERS.

9.3.1. The Notion of Universal Service.

193. Universal service. The most important concern of the Community authorities has been the structural reform of the telecommunications markets. Both regulatory and antitrust mechanisms were developed in order to guarantee the competitive nature of the markets so that the constraints of competition would ensure the satisfaction of the general interest. Nevertheless, some Member States (in particular France and Belgium) imposed the adoption of further mechanisms for the immediate satisfaction of the general interest in the telecommunications sector. This was the origin of the universal service scheme.

Universal service is defined in the Community directives as "a defined minimum set of services of specified quality which is available to all users independent of their geographical location and, in the light of specific national conditions, at an affordable price".[525]

The notion of universal service has a long history in the US, where such a term, even if with different meanings, has always been present in the telecommunications sector.[526] Within the framework of the European Union the term was officially introduced in 1992, at a relatively late stage, when the debate for the full liberalisation was initiated.[527] Once the decision to fully de-monopolised the European telecommunications markets was adopted, the universal service scheme became one of the priorities of the Community

[525] See Article 2(2)(f) Directive 98/10/EC.

[526] See BORROWS, BERNT and LAWTON (1991): "*Universal Service in the United States: Dimensions of the* Debate", WIK, Discussion paper no. 124; and MUELLER, M. (1993): "Universal Service in Telephone History", in *Telecommunications Policy*, vol. 17, no. 5, pp. 352-375.

[527] See SEC(92) 1048, of 21 October 1992.

harmonising policy and one of the leading mechanisms of public intervention in the sector.[528]

194. Universal service scheme. The universal service scheme provided mechanisms to substitute the traditional policy of universalisation of the telecommunications services by the public national monopolies. Traditionally, public monopolies had a mere political responsibility for the provision of the services and no objective control existed to ensure the proportionate and efficient character of the intervention. The elimination of exclusive right and the direct provision of the services by the public authorities led to the lack of the traditional mechanisms to ensure universality, such as cross-subsidies.[529]

The universal service scheme provides an alternative model of public intervention. Intervention is subsidiary to competition in the market, as intervention is only supposed to take place when operators do not satisfy the general interest. It is indirect, as public authorities do not directly provide the services considered of general interest, but imposes on the operators regulatory obligations to ensure such satisfaction. The intervention is objectively based, as it is limited to ensure goals specifically designed as of general interest. Intervention is proportionate, as there is a necessary connection between the general interest objectives and the public intervention implemented to ensure them. Finally, regulatory intervention to ensure the universality of the services is supposed to be non-discriminatory and, therefore, it should not distort the competitive process which has been appointed to govern the sector.

195. Universal access. Article 5 of Directive 98/10/EC states that "Member States shall ensure that all reasonable requests for connection to the

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[528] See for instance COM(96) 73 final, Universal Service for Telecommunications in the Perspective of a Fully Liberalised Environment. An Essential Element of the Information Society, 13.3.96, Brussels, p. 1.

[529] See CAVE, MILNE and SCANLAN (1994): "*Meeting Universal Service Obligations in a Competitive Telecommunications Sector*", European Commission, Brussels, p. 11.

fixed public telephone network at a fixed location [...] are met by at least one operator and may, if necessary to this end, designate one or more operators so that the whole of their territory is covered". Not only access for consumers has to be ensured, but minimum standards of quality are imposed by the directive,[530] and access has to be provided at an affordable price.[531] At the same time recital 11 of Directive 97/51/EC states that "in order to guarantee the provision of leased lines throughout the Community, member States should ensure that at every point in their territories users have access to a minimum set of leased lines from at least one organisation".

It is important to stress that for the first time, universality is not only a political goal but a legal obligation imposed on the Member States by the Community authorities. Furthermore, "Community law [...] not only imposes obligations on individuals but is also intended to confer upon them rights which become part of their legal heritage".[532] Even if it seems clear that the mere wording of the Directives does not create the right for consumers to require operators to provide them access, it creates the right for consumers to claim liability to the State for the lack of implementation of the content of the Directive. With regard to the implementation by the Member States, many of them foresee the imposition of obligations on certain operators for the provision of access in certain areas. Such an obligation does not necessarily grant to consumers a remedy against such operators, but it certainly imposes upon them a liability in case such an obligation is not respected.

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[530] Article 5(1) of Directive 98/10/EC establishes that "the connection provided shall be capable of allowing users to make and receive national and international calls, supporting speech, facsimile and/or data communications".

[531] Article 3(1) of Directive 98/10/EC states that "Member States shall ensure that the services [including access to the fixed network] are made available to all users [...] in the light of specific national conditions, at an affordable price".

[532] See *Van Gend en Loos v. Nederlandse Administratie der Belanstingen*, Case 26/62, 1963 ECR 1, p. 12.

9.3.2. Principles of the Intervention.

196. Subsidiary intervention. It has to be pointed that regulatory intervention through the distribution of obligations among the operators can be implemented exclusively "if necessary" to the end of ensuring universal access to the networks. Article 5(1) of Directive 98/10/EC stresses clearly the subsidiary role of public intervention regarding universal access. Such an intervention can only take place if operators active in the market do not provide such access to all citizens requiring it. If competition in the market ensures the satisfaction of the general interest, then public intervention is to be excluded. As a matter of fact, a significant number of Member States have considered the adoption of a universal service scheme as unnecessary.[533]

A clear case of over-regulation could be found if a Member State would impose on operators obligations regarding access by consumers in a situation in which such access was already universally provided by the operators. Such an intervention would be contrary to the Directive and therefore an infringement procedure could be initiated by the Commission against the Member State.[534]

Member States have introduced different mechanisms in order to ensure the subsidiarity of the intervention. For instance, Spanish legislation foresees that the universal service scheme will only be implemented in case the competent ministry considers that operators active in the market do not ensure the universal provision of access to the network at affordable prices.[535] Furthermore, the ministry will be able to determine the suspension of the universal access scheme if it is considered that access is being provided in

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[533] This was the case of 9 out of the 15 Member States by February 1998, see COM (1998) 101 final, First Monitoring Report on Universal Service, 25.2.98.

[534] Nevertheless, it has been commonly pointed out that Member States suffer pressures to implement universal service schemes for the benefit of particular actors in the market. See for instance KELLY, T. (1995): "Universal Service -An Instrument for regulatory Capture?", in "*Universal Service Obligations in a Competitive Telecoms Environment*", Analysis, Cambridge, pp. 33-44.

[535] See Article 20 ROSP.

competition by operators under similar conditions as those imposed on the operator appointed for the provision of access.[536]

197. Indirect intervention. An other novelty of the new model of public intervention introduced by the Community authorities is the indirect character of the intervention. Public authorities no longer provide themselves the services traditionally considered of public interest. On the contrary, operators in the market are in charge of the provision of such services. Initially, operators provide access to their networks to consumers as their regular activity in the market, following the mechanisms of supply and demand. It has been considered that in principle, such mechanisms should ensure the generalised provision of access to consumers. In the case where operators refuse to grant access to certain consumers due to the lack of economic incentive for such provision, the subsidiary mechanism is implemented.

The universal service scheme does not outlaw the direct provision of the services considered by the public authorities. Nevertheless such a solution is generally discarded for two main reasons. On the one hand, the Directives define a complete scheme for the provision of access by the operators. On the other hand, even if public authorities would directly provide access, they would be subject to all the principles and requirements established by the Community legal frameworks, and in particular to the principle of non-discrimination, in such a way that no particular advantage could be introduced in favour of the public authorities.

The implementation of the universal service scheme in the different Member States foresees different procedures for the designation of the operators in charge of the provision of the uneconomic access services. Such procedures have, in any case, to respect the principles of transparency and non-

[536] See Article 3(2) ROSP.

discrimination. Obligations on access should not distorte the competitive process.

On the one hand, universal service obligations should never become an excessive burden on an operator which then disadvantages it in the competitive process. Therefore, obligations for the uneconomic provision of access should not be imposed on new comers struggling to initiate their activities, but on established operators for which such an obligation does not impede the regular development of their activities. That is why the Community directives make continuous references to the provision of this kind of services by operators with significant market power.[537] As a matter of fact, most of the Member States which have implemented a universal service scheme have opted for the initial designation of the incumbent operator for the universal provision of access in all the national territory.[538]

On the other hand, and this might not be so evident, the designation of an operator for the provision of uneconomic access services should not benefit such an operator and grant it a privileged position in the competitive market.[539] The beneficial effects of the provision of universal services has been widely studied.[540] Corporate reputation benefits from the provision of uneconomic access, as well as brand recognition and marketing, due to ubiquity. Finally, the

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[537] See for instance Article 13(1) of directive 98/10/EC.

[538] This is the case of Spain, where Telefónica was designed by the third Transitory Provision of the General Telecommunications Act of 1998 for the universal provision of access to consumers until December 31 2005. France Telecom was also charged with this obligation by Article 35(1) of the Act on the regulation of telecommunications of 1996. Furthermore, in Denmark Article 6 of the Act on Universal Service Obligations requires a nation-wide market share over 50% in a particular market in order to impose universal service obligations, and in Austria the operator with a higher market share will be the one the one which will suffer the burden if no other operator is interested.

[539] See for instance BLACKMAN, C. (1995): "Universal Service: Obligation or Opportunity?", in "*Universal Service Obligations in a Competitive Telecoms Environment*", Analysis, Cambridge, pp. 1-8.

[540] Particularly interesting are the studies undertaken in the UK. See Analysys (1995): "*The Cost, benefits and Funding of Universal Service in the UK*", OFTEL, London, pp. 8-16; and OFTEL (1995): "*Universal Telecommunications Services. A Consultative Document on Universal Service in the UK from 1997*", OFTEL, London.

provider has a more complete knowledge of consumers patterns. More decisive might be the fact that being designated as universal access provider increases the market share of the operator, often at the expense of the other operators which finance the provision. This market share might decisively increase the efficiency of the operator as it could benefit from the important economies of scale which the sector presents. As a result, once new operators acquired a more stable position in the market, they could be willing to increase their market share through the provision of uneconomic access under the universal service scheme.

The automatic designation of the incumbent as the access provider might be discriminatory in the sense that it could ensure for it a market share financed by the competitors. A similar effect might be the restriction contained in the French legislation according to which only those operators who can provide universal service throughout the entire territory of the nation can be designated for the provision.

The Legislation in some Member States foresees the implementation of competitive mechanisms for the designation of the operator in charge of the provision of uneconomic access services. In Spain and Germany, for instance, tenders will be organised for the designation of the provider.[541] In such a way, not only the procedure will be transparent and non-discriminatory as required by Directive 98/10/EC, but at the same time the cost of the provision of the service is expected to be reduced by the competitive bidding. In case no operator shows interest in the provision of the service, the competent ministry will impose the obligation on an operator with significant market power in the market under consideration.

[541] For an evaluation of the use of tenders for the determination of the universal service provider *vide* CAVE, MILNE and SCANLAN (1994) p. 59 (*supra* footnote 529).

198. Objective and proportionate intervention. The new model of public intervention for the protection of the general interest introduces objectivity. The traditional model of direct intervention often did not differentiate the mere managing of the service from the measures driven by general interest objectives. As a result, it was not necessary to justify the general interest involved in a particular action. Broad definitions of the general interest were common and no objectively connected schemes were usually associated to them.

The indirect intervention of the public authorities required a radical reform of the relation between the general interest declarations and the measures implemented to protect it. Indirect intervention has forced, on the one hand, the precise definition of the objectives considered to be of general interest. On the other hand, the measures implemented to ensure the satisfaction of the general interest have to be directly linked to the objectives promoted and objectively justified.

Even if in the last decades universalisation of the telecommunications networks was a common general interest objective in all the Member States, a clear definition of the objective was usually lacking. The network standards to be ensured in all the territory were not clear, nor the reasonability of the demands for access in remote areas. The universal service scheme, on the contrary, required the precise definition of the general interest objectives regarding access to the network by consumers. Only such definition would legitimate the imposition of legal obligations on operators to ensure the satisfaction of the general interest.

Which services were to be included under the universal service scheme generated one of the most important debates in the process of reform of the sector. One party defended that access should only be ensured to a network capable of providing the most basic services, those services already mature and with a high degree of penetration (around 75%) that is basic telephony and the

most basic data services such as facsimile.[542] The other party advocated for ensuring access to a network with broader capabilities in order to promote the fast development of the new services of the information society. In such a way, network development would proceed ahead of demand.[543]

Community authorities finally adopted the most restrictive position and included under the universal service scheme the obligation for the Member States to ensure access to a fixed public telephone network infrastructure of a quality which supports in addition to speech, data communications at rates suitable for access to on-line information services.[544] Nevertheless, the Community Directive recognises that "the concept of universal service must evolve to keep pace with advances in technology, market developments and changes in user demand", and it was foreseen that a first review of the services included under the scheme would take place in 1999.[545]

Article 4 of Directive 98/10/EC established the prohibition for Member States to include under the universal service scheme other services considered of general interest.[546] It did not exclude, however, the creation of parallel schemes for those services, as long as in accordance with community Law. Some Member States as France or Spain have reacted to the narrow definition of the Community authorities by creating such parallel categories and schemes of indirect intervention. In this way, services not included in the Community category of universal service, can be the objet of a similar parallel regime.

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[542] This was the position of most of the operators and some Member States, led by the UK. See for instance Analysys (1997): "*The future of Universal Service in telecommunications in Europe*", European Commission, Brussels.

[543] Some Member States led by France as well as the trade unions promoted the inclusion of ISDN networks or access to Internet under the universal service scheme.

[544] See recital 4 and Article 5(2) of Directive 98/10/EC.

[545] See recital 1 and Article 31 of Directive 98/10/EC.

[546] Some Member States, however, have included other services. This is the case of Belgium, where tariff discounts granted to journalists and the Belgium agency have been pointed out by the Fourth Report on implementation as being not in conformity with the EU framework. In Italy, financing for research might also be included.

Regarding the obligations imposed on the operators, they have to be objectively linked to the satisfaction of the general interest objective precisely defined by the public authorities. Furthermore, the obligations imposed on the operators have to be proportionate to the general interest objectives pursued by the public authorities.

One of the most important novelties introduced by indirect intervention is the need to evaluate the cost for the operator of the obligations related to the general interest objectives. As it happened with interconnection, the cost allocation is particularly difficult in the telecommunications industry.[547] As it is stated by Article 4 of Directive 98/10/EC, operators have to specify the elements for which funding is requested. Directive 97/33/EC further develops the mechanisms established to ensure the proportionality of the obligations imposed on the operators and the costs of such obligations. Annex III of the latest directive states that "the cost of universal service obligations shall be calculated as the difference between the net cost for an organisation of operating with the universal service obligations and operating without the universal service obligations".[548]

Important divergences can be observed in those Member States where the costs of the provision of universal services has been evaluated.[549] Even if in every case the cost was below 6% of the revenues of the incumbent operator (usually in charge of the provision of the service), some Member States like France or the Netherlands fixed the cost at around 5.5% of the revenues of the

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[547] For an analysis of the difficulties faced regarding the determination of the costs of universal service obligations *vide* CAVE, MILNE and SCANLAN (1994), pp. 27-43 (*supra* footnote 529); and NEU, STUMPF, NETT and SCHMIDT (1997): "*Costing and Financing Universal Service Obligations in a Competitive Telecommunications Environment in the European Union*", European Commission, Brussels.

[548] The Commission provided some guidelines to the Member States in COM(96) 608, Commission Communication on Assessment Criteria for National Schemes for the Costing and Financing of Universal Service in Telecommunications and Guidelines for the Member States on Operation of such Schemes, 27.11.96, Brussels.

[549] See First Monitoring Report p. 32

incumbent, while the UK fixed it at around 1% and Spain at around 3%. It is hard to understand how the universal service costs are higher in the Netherlands, with its very propitious geography and high penetration values, than they are in Spain where important geographic difficulties are faced, and the penetration rate is significantly under the EU average.

In the French case, the financial burden impose on the new comers might become a substantial barrier to entry according to the Commission,[550] which initiated a formal procedure against France in the Autumn of 1997 regarding the universal service scheme. New comers criticised the methodology used to calculate the net cost, as the market benefits which accrue to FT as the universal service operator might have not been fully taken into account. As a result, the costs for the provision of universal service by France Telecom were fixed in FF 4,8 billion for 1997 (5.5% of FT revenues on fixed telephony) and FF 6 billion for 1998 (7.3% of FT revenues). Despite the fact that measures on tariff re-balancing reduced the cost for 1999 to FF 3 billion, the Commission continued the procedure and sent a reasoned opinion.[551]

199. Non-discrimination. A further requirement of the regulatory intervention for the protection of the general interest, and in particular with regard to the promotion of universal access to the telecommunications networks by consumers, is the non-discrimination between operators. Such a requirements is defined by Article 5(1) of Directive 97/33/EC and Article 3(1) of Directive 98/10/EC. Furthermore, non-discrimination includes also neutrality between technologies.

Discrimination can take place through different mechanisms such as the designation of the operator in charge of providing the service, which can benefit certain operators against other, or impose an excessive burden on a

[550] See fourth Report, p. 85.

competitor. In any case, the most delicate issue in the universal service scheme is the distribution of the obligations for the financing of the provision of the service.

Firstly, the obligation to provide universal access in a particular area can impose a burden on the designed operator and hinder its competitiveness. This will not always be the case, as the provision of universal access might have a very reduced cost and, as it was shown earlier, the provider of such an access obtains intangible benefits which might counterbalance the costs faced. In any case, if the provision of the service is an excessive burden which distorts competition in the market, the Community Directives require the introduction of measures devoted to the elimination of the distortion

Community directives consider appropriate the distribution of the economic burden among the competitors, in such a way that none of them is benefited or damaged by the public intervention. This is not the only solution, as it might also be possible for the public authority to provide directly the financing for the provision of the uneconomic service. Such a solution, nevertheless, is incompatible with the actual trend of reduction in public expenditure and with the traditional consideration of the telecommunications sector as a revenue making.

In any case, the distribution of the economic burden among the competitors has to be non-discriminatory. The Community directives foresee two different schemes for the distribution of the burden among competitors. On the one hand, it was foresaw the possibility of introducing a supplementary charge added to the interconnection charge. Such a possibility seemed better adapted to a situation in which the incumbent not only maintains a high market share, but also is the main (or even only) provider of universal access. The implementation of the system would be more difficult as the market would be

[551] See Press release IP/99/494, 13.7.99.

more fragmented as well as the provision of universal access is the responsibility of more operators. As a matter of fact, most Member States have opted for the second possibility, which consists in the establishment of a specific mechanism run by an entity independent from the beneficiaries, which would determine the costs of the provision of the service and distribute it among the operators, creating a universal service fund.

The first element to determine is the identity of the operators required to share the economic burden of universal access. Article of Directive 98/10/EC restricts the ambit of the obligation to the "organisations operating public telecommunications networks and/or publicly available voice telephony services". The Commission stressed the need to exclude such a burden to operators running private networks, or value-added services. Some Member States foresee the possibility of temporally excluding some operators from contributing in order to promote the introduction of innovative services as well as to ensure the promotion of competition.[552]

The second important element is the determination of the share of the burden to be faced by each operator. The Commission has stressed that such distribution should not distort investment initiatives and economic efficiency, nor impose "double contributions".[553] Furthermore, it has been stated that national schemes should ensure that the criteria chosen to determine the burden share of eligible organisations does not have a disproportionate or discriminatory effect on particular players".[554] As a result, the burden should be distributed according to objective criteria based on the position in the market of

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[552] In Austria, operators with an annual turnover under ATS 250 million will not be required to contribute and a similar rule applies in Belgium. In Germany, only operators with a national market share over 4% are bound. In Italy, for instance, only the most successful new comers to the fixed telephony market have been forced to participate in the financing of the universal service.

[553] See COM (96) 608, p. 17. Double contributions exist when operators contribute directly for the services they provide and indirectly through the payments made for services provided to them (such as leased lines).

[554] *Ibid.*

the operators. Indicators such as revenues, call minutes, number of subscribers or market share were proposed by the Commission.[555]

200. Transparency. The latest requirement imposed by the Community directives on the universal service schemes implemented by the Member States is transparency. Such a requirement is introduced in order to ensure the efficacity of the other requirements such as objectivity, proportionality and non-discrimination. Since most of the decisions regarding the scheme are highly discretionary, it is necessary to allow operators, as well as consumers, to control that soundness of the decision-making process. Community directives impose not only the principle,[556] but also specific obligations related to transparency.

Firstly, even if the cost of the provision of universal access is to be calculated by each operator suffering it, the calculation has to be audited by an independent body, approved by the national regulatory authority, and made available to interested parties.[557] Secondly, when such costs are to be shared, the principles governing the distribution of the burden and the details of the mechanism used are also to be made available to the interested parties.[558] Finally, an annual report has to be published by the national regulatory authorities giving the calculated cost of universal service obligations and identifying the contributions made by all the parties involved.[559]

The national universal services schemes had to be communicated to the Commission according to Article 3 of Directive 96/19/EC, so that Community

[555] In Austria, for instance, the criteria is the market share, in Belgium the operators' turnover in the particular market

[556] See Article 5(1) of Directive 97/33/EC and Article 3(1) of Directive 98/10/EC.

[557] See Articles5(3) and 14(2) of Directive 98/10/EC.

[558] See Articles 5(5) and 14(2) of Directive 98/10/EC.

[559] See Article 5(5) of Directive 98/10/EC.

authorities would have the chance to verify the compatibility of the drafts with the Treaty.

9.4. CONCLUSIONS.

201. Different market structures. Public intervention regarding network access has necessarily to take into account that such access might take place in markets with decisive structural differences. Public intervention should be adapted to such differences in order to avoid distortive results which not only do not effectively ensure the satisfaction of the general interest but actually obstruct its obtention.

The process of the liberalisation of the European telecommunications markets consists in the substitution of the traditionally publicly ruled activities by private initiative governed by the mechanisms of competition. This is the leading principle of the reform and it should always inform public intervention in the market. Nevertheless, it has to be taken into account that the particular characteristics of the telecommunications sector do not always ensure the efficacity of the constraints of competition.

Firstly, on certain occasions effective competition is excluded from the market. Two are the fundamental cases in which this happens. On the one hand, it has been analysed that the provision of access in some remote areas might not be economically interesting for any operator. In this case, no market exists, and public intervention has to ensure the availability of the most basic telecommunications services. On the other hand, it is sometimes the case that in a particular market segment a very reduced number of operators might provide network access to consumers, maybe only one, as the traffic generated by the consumers does not ensure the recovery of the costs generated to a significant number of operators. In such a case, no effective competition is possible, or even potential. Public intervention might be then necessary in order to exclude

exploitative practices against consumers, but also exclusionary practices against competitors requiring access to the network for the provision of their services.

Secondly, in some markets there is room for competition and in fact the elimination of the exclusive rights has allowed new comers to start developing their networks. Nevertheless, it has already been pointed that the installation of networks with full coverage requires time. So effective competition will only be present in some markets after a period of a number of years. In the meantime, the incumbent can abuse its market power and impose exploitative as well as exclusionary practices. Public authorities have to take into account that this is supposed to be a temporary situation and that intervention implemented to speed up the emergence of competition should never obstruct the development of competition in the market.

Finally, in some network markets effective competition appeared as soon as exclusive rights were banned. Public intervention has to be then conscious of its subsidiary role, avoid pervasive intervention, and limit itself to the regular intervention devoted to obstruct behaviours aimed at eliminating competition from the market.

202. No competitive markets. Regulation seems particularly necessary in order to ensure the universal availability of network access in the whole territory of the Union at an affordable price. As it has been shown, it might not always be necessary to implement the scheme foreseen by the Community directives, for it might be the case that in a particular moment operators are in the position to provide universally access to the networks considered of general interest under the constraints of competition. In any case, such schemes have to be maintained, even if not implemented, as modifications in market conditions which occur or the evaluation of services considered of general interest might change.

The ONP framework provides a scheme which ensures on the one hand effectivity and on the other guarantees its procompetitive character. The scheme provides enough mechanisms so that Member States can ensure the universality of access. Such is the case of the possibility of imposing on the operators as obligation to provide access in uneconomic conditions. At the same time, the leading principles of the ONP framework, proportionality, non-discrimination and transparency, obstruct the implementation of policies which distort the competitive process.

203. ONP and permanent regulation. Just as there are situations in which no operator might be interested in the provision of access given how uneconomic it would be, there are situations in which only one operator might provide such an access. This is the situation of those network elements which are to be considered essential facilities by the rules on competition, that is, those facilities for which duplication is not considered viable due to legal, physical or economic conditions.

In any case, the network elements for which duplication, and therefore competition is not possible are nowadays exceptional, due to de-monopolisation, technical evolution, and the eclosion of traffic generated by the Information Society. As a result, any public intervention devoted to impose constraints regarding access to such network elements should be based in a firmly justified determination of the lack of potential competition in the market.

One again, the ONP framework provides mechanisms in order to substitute the constraints of competition by constraints imposed by public authorities. As in the case of creation of the market, the ONP framework has the tendency to be at the same time effective and procompetitive. Once again, public intervention might not always be necessary under these conditions, as operators might, by different reasons, not abuse of it. Nevertheless, mechanisms of subsidiary intervention will be necessary in order to ensure that

factual monopolist do not implement exploitative practices nor exclusionary strategies. Furthermore, such mechanisms should be of a permanent character, as the market structure cannot be expected to evolve over time.

204. Competitive markets. The elimination of the exclusive right for the installation of telecommunications infrastructures has allowed hundreds of new operators all over Europe to initiate the installation of their own infrastructures. Most network segments are being duplicated and in the most interesting market segments a significant number of parallel networks is being developed. As a result, it is difficult to argue that, in general, telecommunications infrastructures are essential facilities or, in other words, markets in which there is no room for effective competition.

Due to the subsidiary character of the regulatory framework on network access, the application of such rules in competitive markets should be excluded, as the regular mechanisms of competition should already impose the necessary constraints on the operators for the provision of access at fair conditions.

Nevertheless, the development of competition in most of the infrastructures markets will take time, as the installation of comprehensive networks requires a significant amount of time. In this situation public intervention might not be indispensable, as the regular mechanisms of the market would ensure the emergence of effective competition. However, it has been considered that public intervention would accelerate the emergence of competition and at the same time ensure the immediate protection of the general interest in the transitory period.

205. ONP and effective competition. As it has been studied, the regulatory framework on network access has as its main objective the imposition on operators of the constraints which effective competition would impose on them. Nevertheless, in some network markets effective competition

appeared as soon as the exclusive rights were eliminated, as they were particularly profitable and the infrastructures could be easily installed (I some cases alternative infrastructures existed even before liberalisation). This is the case of the main segments of the backbone networks.

In those markets, the constraints imposed by public authorities are redundant and therefore unnecessary. Furthermore, such constraints easily distort competition in the market, as they impose burdens on certain categories of operators to the benefit of those operators who do not suffer the intervention. In this way efficiency is not always rewarded and inefficient operators might survive in the market

The Community regulatory framework foresees the possibility for the Member States to exclude the application of the regulatory obligation in those markets were effective competition exists, as well as the appropriateness of such exclusion. Nevertheless, no regulatory mechanisms are imposed by the directives on the Member States to ensure that such exclusion takes place as competition emerges. As a conclusion, the Community regulatory framework lacks an efficient mechanism for the elimination of unnecessary regulation on network access and to ensure the innexistence of over-regulation.

206. Transitory regulation. More complicated is the situation in those markets in which even if there is space for network competition, it will take a significant period to emerge as the installation faces difficulties for different reasons (significant investments, access to rights of way etc.) or just requires time in order to become comprehensive.

Regulation in these markets has faced a complicated option. On the one hand, access could be facilitated in order to promote the provision of services by operators without infrastructures. In this way, consumers would promptly notice the reform of the sector as they would have a significant number of service providers at their disposal. Nevertheless, in such a way network

competition would be disadvantaged as investments in the installation of networks would not be as profitable. As a consequence, effective competition in the network markets could be delayed and even obstructed by the regulatory obligations on access.

On the other hand, the option could have been not to excessively facilitate access by competitors in order to promote investments in infrastructures. Effective competition in such markets would have ensured competition also in the service markets. In this case, however, the effects of competition would have been delayed in time, as consumers would have only noticed the effects of the reform years after the de-monopolisation.

The Community authorities, followed later by the national authorities, opted for an intermediate approach. Even if access by services providers was facilitated, the objective has been to leave enough space for the investment in parallel infrastructures.

In any case, the Commission's proposals for the reform of the telecommunications directives foresees specific mechanisms for elimination of regulation on access as competition emerges and imposes effective pressure on all the operators. NRAs would be forced to analyse the markets and in case such effective competition is identified, regulatory obligations should be lifted.

CHAPTER 10

CONCLUSIONS: FROM REGULATION TO COMPETITION?

SUMMARY: 10.1. Introduction. 10.2. Complementarity relationships. 10.3. Counter-balance relationships. 10.4. Conclusions.

10.1. INTRODUCTION.

207. Public intervention in liberalised markets. The process of liberalisation has put an end to the public monopoly, the traditional instrument of public intervention in general interest sectors. De-monopolisation and privatisation, nevertheless, do not eliminate the relevance of telecommunications and other network industries for the general well-being and the economic development of modern societies.

As a consequence, it has been necessary to substitute direct intervention by new instruments of public intervention compatible with the competition in the market whilst at the same time being effective in the protection of the general interest.

From this perspective, the rules on competition provided mechanisms to ensure consumer welfare as well as the protection of the competitive character of the markets. However, such rules do not seem fitted to ensure the satisfaction of those general interest objectives which go further than mere efficiency in the provision of products or services. At the same time, the rules on competition have been designed to protect competition, but not to create it.

As a consequence, other instruments of public intervention were needed. Economic regulation was the answer. Economic regulation can be understood as the continuous and concentrated control of the market by public authorities through the imposition of legal obligations on the private operators, according to their position in the market, in adaptation of the abstract obligations defined by the Legislator, with the objective of ensuring the adaptation of the functioning of the markets to the general interest objectives.

It has been shown that both the rules on competition and sector specific regulation provide mechanisms for public intervention to ensure access to the telecommunications networks to promote competition as well as to ensure the universal provision of the most basic telecommunications services. It has been shown at the same time, though, that the application of both instruments involves limitations as well as risks. The adequate and balanced co-ordination of both mechanisms could, on the one hand, overcome the limitations of each instrument, and in this way ensure the effectivity of public intervention, and, on the other hand, elude the risks derived from failures in the enforcement of each instrument of intervention.

208. Complementarity. Competition Law and sector specific regulation can complement each other in order to ensure the effectivity of public intervention as regards network access. Such complementarity derives from the different nature of both instruments, which entails different mechanisms of intervention. At the same time, complementarity is favoured by the fact that sector specific regulation on access was somehow inspired by the structure and the principles of the rules on competition regarding abuses of dominant position.[560]

On the one hand, the ONP framework complements the rules on competition dealing with network access. Firstly, the ONP framework expands the obligations defined by the essential facilities doctrine to situations in which such doctrine cannot be applied as some competition, even if not effective competition, is possible in the market. It even expands the application of such principles to operators that cannot even be considered in a dominant position. Secondly, the ONP framework provides regulatory mechanisms of intervention which go further than the competition Law mechanisms. Such mechanisms not only ensure the efficacity of the regulatory framework, they also ensure the efficacity of the rules on competition, as they provide the necessary tools and information in order to apply it.

On the other hand, the rules on competition complement the ONP framework. The nature of regulatory intervention generates the apparition of loopholes in the intervention. Firstly, the *ex ante* definition of the broad regulatory obligations makes possible the existence of conflicts that were never foreseen by the regulators. Secondly, the adaptation of the broad obligations to the specific conditions of each operator can be obstructed by different reasons (capture of the regulator, lack of resources etc.). As a result, the regulatory framework on network access might not provide a precise solution in a

[560] *Vide supra* Chapter 9.2.3. Compulsory Access.

particular conflict. The different nature of the rules on competition, based on horizontal, very broad prohibitions, ensure the existence of a "safety network" for those occasions in which regulation fails to obstruct anticompetitive behaviours.

209. Counter balance. The interaction between the rules on competition and the sector specific regulation not only ensures that they complement each other, but also allows them to counterbalance some of the negative tendencies that can be identified in their application to network access conflicts.

The very same existence of the sector specific regulation on network access counterbalances the already discussed regulatory tendency of the European rules on competition. The ONP framework provides mechanisms to ensure access that avoid the need for the rules on refusal to deal to be over-stretched and denaturalised.

As the ONP framework has taken the lead as the main instrument of intervention regarding network access, and given that it is well known the tendency of regulation to expand, the most important counterbalance role is for the rules on competition. Competition Law, particularly Community competition Law, provides mechanisms for the obstruction of public measures which obstruct competition in the market. Article 86 of the EC Treaty (former art. 90) and the *effet util* doctrine developed by the Commission and the ECJ allow the Commission to intervene against State measures of a regulatory character which obstruct competition.

10.2. COMPLEMENTARITY RELATIONSHIPS.

10.2.1. Regulation complements antitrust.

210. General. As it has been pointed out, the ONP framework was launched by the European Commission following the principles embedded in

the essential facilities doctrine as originally received in Europe, and in particular, non-discrimination. It is interesting to note how the most important regulatory intervention in the telecoms industry, network access, has been somehow transplanted from the US through the irregular path of competition Law. This fact determines the relation between both instruments of intervention.

The ONP framework has been developed as a complement to the rules on competition, in order to ensure mechanisms of intervention for those cases in which competition Law was not applicable and, furthermore, in order to provide more powerful mechanisms even for those cases in which the rules on competition were applicable. The structure of the antitrust figure of abuse of dominant position has been transplanted to the regulatory framework through the definition of the category of operator with significant market power, and the imposition of asymmetric regulatory obligations as regards access to the operators with such power. The Commission's proposals after the 99 Review confirm this analysis.

As a result, the ONP framework has advanced the line of intervention with regard to network access, but in general, such a line runs in parallel to the line drawn by the rules on competition. The regulatory obligations on network access expand the obligations imposed by the rules on competition as interpreted by the Commission to a wider category of operators. At the same time, the regulatory framework defines with more detail the content of such obligations. In such a way, the efficiency not only of the regulatory framework, but also of the antitrust rules, has been increased.

211. Access to essential facilities. The essential facilities doctrine, as interpreted by the ECJ, provides a mechanism for imposing the obligation on an operator to provide access to its network with no-discriminatory

conditions.[561] The exceptional character of such an obligation, however, required a regulatory complement.

Firstly, the complexity of the network industries complicates the comparison of the access conditions and, therefore, the evaluation of their non-discriminatory character. Regulatory obligations imposed *ex ante* can facilitate such an evaluation. This is the case of the obligation to implement accounting separation between different activities, as well as the obligation to respect certain accounting principles that ensure the transparency of the accounting. As a conclusion, the application of the essential facility doctrine would be obstacled without these regulatory obligations. As a matter of fact, the Commission stated in the Access Notice that it would apply the competition rules building on the ONP directives,[562] and that the Commission recommendations concerning accounting requirements and transparency will help to ensure the effective application of Article 86 [now article 82]".[563]

Secondly, the mere proscription of the refusal to grant access is not sufficient, as the lack of competition does not allow the market mechanisms subsequently to determine the access conditions. As a result, further mechanisms of intervention are necessary in order to ensure network access. The rules on competition do not provide mechanisms for the prescription, in case of lack of agreement, of the access conditions. Competition Law proscribes anticompetitive behaviours, but is not supposed to prescribe the behaviour of the operators in the market. Furthermore, even in case a competition authority would be tempted to adopt such a regulatory role, it would face the difficulties derived from the lack of mechanisms for the

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[561] *Vide supra* Chapter 8.5. Refusals to Grant Network Access.

[562] See Notice on the application of the competition rules to access agreements in the telecommunications sector. Framework, relevant markets and principles, OJ 1998 C 265/2, of 22.8.98, para. 24.

[563] *Ibid.* Access Notice, para. 116.

continuous control of the markets and the adaptation of the conditions to the new circumstances.

As a consequence, the essential facilities doctrine provides an antitrust mechanism to obstruct an anticompetitive behaviour, but it cannot by itself resolve all the potential conflicts on network access, and for this reason, a complement of the regulatory framework is necessary.

212. Access to non-essential facilities. The complementative role of the regulatory framework on network access is even more important with regard to non-essential facilities. Regulatory obligations on access can be imposed in relation to bottlenecks which cannot be considered essential facilities and, furthermore, on non-dominant operators.

As was shown following the most recent decisions of the Community Courts, the most aggressive intervention on network access based on the essential facilities doctrine is restricted to very exceptional cases. Access to the telecommunications networks can not be granted as a general competition rule to the non-essential telecommunications facilities.[564] Regulation, nevertheless, is more flexible and the ONP framework foresees the expansion of the interconnection and access obligations to network facilities that under no concept can be considered essential, that is, unavoidably monopolised. At the same time, access obligations are imposed not only on dominant operators, but also on operators with significant market power, a category that includes operators that under no circumstance could ever be considered dominant under the rules on competition. The new regulatory framework proposed by the Commission eliminates this category but, somehow, opens the door for a regulatory strategy against oligopolistic structures in the telecommunications markets.

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[564] *Vide supra* Chapter 8.4. The Limitations of Essential Facilities Doctrine.

The wider ambit of application of the regulatory obligations allows to make use of such mechanisms for intervening in situations out-side of the scope of the rules on competition. In this way, it is possible for public authorities to face the particular challenges of the exceptional transition from monopoly to competition. It has been sustained that compulsory access to non-essential telecommunications facilities could foster the emergence of competition in the services markets.

At the same time, regulatory intervention might be necessary to face the oligopolistic market structures which are being created, slowly though, in the traditional fixed telephony markets or the new electronic communications markets of mobile communications and digital television.

The flexibility of the regulatory mechanisms could allow public authorities to intervene in access conflicts related to the existence of bottlenecks which might not be essential facilities, or even might not grant a dominance according to competition Law standards, but which certainly grant a market power which could determine the evolution of the telecommunications markets.

213. The case of mobile communications. This is the case, for instance, of the market power of the mobile operators against the biggest number of fixed operators regarding call termination in mobile networks, particularly in the framework of convergence between fixed and mobile communications. Even if the rules on competition provide mechanisms to obstruct collusive agreements and foresee the existence of collective dominance, regulatory mechanisms have proved more effective in order to obstruct distorsive behaviours of mobile operators.

Article 7(2) of Directive 97/33/EC allows NRAs to declare mobile network operators as with Significant Market Power in the national interconnection markets, and as a consequence, be covered by the regulatory

obligations on cost-orientation and cost accounting.[565] NRAs such as the Italian AGCOM[566] and the French ART[567] declared with Significant Market Power in the interconnection market not only the leader (which in the Italian case would clearly have been considered dominant under the antitrust standards) but also the second mobile operator (which in the Italian case had a mere 18% market share in the interconnection market and around 25% in the mobile market).

The Italian case is particularly interesting, as the intervention of the NRA was followed days later by the intervention of the Italian competition authority (AGCM) in order to put an end to a collusive agreement between TIM and Omnitel for the price-fixing of termination prices.[568] A very important sanction was imposed as a result of the anticompetitive behaviour, but the competition authority refrained from adopting a regulatory approach and no obligation to follow determined prices was adopted. The determination of the pricing criteria was left for the NRA, which had adopted the decision to impose cost-oriented prices just some weeks before.

The new regulatory framework proposed by the Commission allows for the adaptation of the regulatory intervention to the specific characteristics of each product and geographic market. In case a market analysis leads to the individuation of a market failure in a specific market, regulatory intervention will be possible. This flexibility avoids some of the problems of the liberalisation regulatory framework, which was rather rigid, as it was mostly designed for the regulation of access to the incumbent's fixed telephony network.

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[565] See the document published by DGXIII on 1st March 1999, "Determination of Organisations with Significant Market Power (SMP) for implementation of ONP Directives", as well as the considerations of OFTEL (1998): "Identification of Significant Market Power for the Purposes of the Interconnection Directive".

[566] Decision no. 197/99 of AGCOM of 7 September 1999.

[567] Decision no. 99-823 of the ART of 30 September 1999.

[568] Decision in the case I372, TIM-OMNITEL Tariffe fisso-mobile, of 28 September 1999.

214. Universal service. The rules on competition provide mechanisms for the protection of the competitive process in the market, and in Europe, even for the imposition of certain positive behaviours in the market. Nevertheless, it has been pointed out that competition Law lacks the mechanisms to impose the provision of a service in case such service is not profitable for the provider. The rules on competition do not create markets where there are no conditions for their existence. As a result, such rules cannot ensure all citizens access to the most basic services.

This does not mean that such an objective is incompatible with the rules on competition. On the contrary, the protection of the competitive process has as its ultimate goal the promotion of consumer welfare, as competition lowers prices and fosters the providers' efforts to meet the consumers' demands. Furthermore, some of the mechanisms established by the rules on competition (such as excessive pricing) directly protect consumer welfare. As a consequence, whilst the rules on competition do not ensure access to telecommunications networks and services, they do promote it.

The ONP framework has introduced a complement to the rules on competition in order to provide mechanisms which give this further step and not only foster but ensure citizens access to the network through the direct imposition of obligations. It is important to note, though, that these obligations create a market which otherwise would not exist, and respect the fundamental rules governing supply and demand in the market. The universal service scheme, in principle, is not an exception to the market, but an intervention to complement it, respecting its basic laws.

10.2.2. Antitrust complements regulation.

215. The role of antitrust. The Access Notice recognises that the application of the regulatory mechanisms established by the ONP framework

would often exclude the need to apply the competition rules on refusal to deal. The more detailed content of the regulatory framework on network access and the more powerful mechanisms of intervention established by the Directives should initially be enough to ensure the satisfaction of the general interest. As stated by the Commission "the proper application of these rules should often avoid the need for the application of the competition rules".[569]

Nevertheless, the rules on competition might play an important role in relation to network access as a "safety network" for those occasions where the regulatory framework does not ensure the obstruction of anticompetitive refusals to grant access.

216. Filling loopholes. The very same nature of regulation favours the existence of loopholes. There are two main reasons for this. On the one hand, regulatory obligations are defined *ex ante* (it can be the case that the regulatory intervention takes place as a conflict resolution, that is, *ex post*, but the attribution of the competence to solve the conflict as well as the criteria to solve the conflict have to be established *ex ante*). As a result, there might be conflicts which are not foreseen and for which no solution is provided. On the other hand, regulatory obligations often have to be adapted to the specific circumstances of each operator in the market. Different reasons might obstruct such an adaptation and therefore eliminate the efficacity of the general regulatory framework.

Loopholes in the regulatory framework are particularly probable in the telecommunications regulatory framework, and particularly with regard to network access.[570] The high complexity of the market and the lack of experience in de-monopolised markets causes uncertainty. Furthermore, the

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[569] *Vide* Access Notice, para. 58 (*supra* footnote 562).

[570] See MARTÍNEZ LAGE, and BROKELMANN (2000): "The Respective Roles of Sector Specific Regulation and Competition Law and the Institutional Implications", in "*European Competition Law Annual 1998. Regulating Communications Markets*", Ehlermann and Gossling Ed., Hart, pp. 637-665.

telecommunications market is characterised by its fast evolution. The regulatory framework might become outdated at a fast speed as technologic progress and market evolution modify the reality under regulation.

This seems to be the case in relation to the tendency towards convergence. Technological evolution is creating new requirements of access firstly between different telecommunications networks (fixed and mobile, for example) and secondly between telecommunications, broadcasting and computer networks.

As a matter of fact, one of the leading principles of the reform of the ONP framework in the 99 Review process was the desire to establish wide principles in order to avoid being outdated in the short term. The Commission proposal to establish regular mechanisms of definition of the markets in which intervention is necessary will reduce the loopholes. In any case, there will always be new conflicts not foreseen by the regulatory framework.

In many occasions, the regulatory framework requires an active intervention of the public authorities in order to ensure its efficacity. Such is the case, for instance, of the intervention to solve access disputes. Even if the ONP framework foresees a solution to a particular conflict, it might be the case that the implementation of the solution faces obstacles that finally exclude the efficacity of the solution foreseen. The complexity of the conflicts, or the mere lack of resources of the national authorities in charge of the implementation of the ONP framework, might lead to a mistaken application of the regulatory rules on access, or even to no intervention from the national authorities.[571]

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[571] In some Member States market players have denounced that the NRA have insufficient powers (such seems to be the case of Belgium, Luxembourg, France, Germany, Denmark, Austria or Portugal), while in other States it has been common the criticism that NRAs do not make the most of its ability in exercising all the powers assigned to them (for instance in the UK, Sweden or Spain). See COM(99) 537, of 11 November 1999, "Fifth Report on the Implementation of the Telecommunications Regulatory Package", p. 15.

Furthermore, the phenomenon of regulatory capture has been well studied. Regulatory authorities suffer necessarily major pressures from the actors involved in the regulatory process. As regulatory authorities are usually independent authorities in close connection to the regulated industry, they are particularly prone to be "captured" by certain factions of the industry and might be forced to ignore the regulatory framework. The political weakness of most of the NRAs often allows the national champions to obstruct the activity of the regulators even through pressures by other governmental bodies such as the competent Ministries or directly by the political parties which often have a closed control of the NRAs.

217. Antitrust as a "safety network". The rules on competition can complement the regulatory framework on network access filling the loopholes that might exist. The horizontal and general nature of the rules on competition allow public authorities to intervene even against anticompetitive behaviours which had been never foreseen by the authorities. At the same time, the different level of government reduces the possibilities of capture both of the national regulatory authorities and the competition authorities at a national and at a Community level.

As a matter of fact, the Commission, in the Access Notice foresees expressly the possibility of the application of the Community competition rules to network access conflicts in case national regulatory authorities cannot ensure a satisfactory solution in a six months period.

For instance, in 1998 the Commission launched an investigation on the interconnection prices between fixed and mobile networks based on the Community rules on competition.[572] The Commission was particularly concern with the high rates for the call termination by mobile operators. Such operators are not bound by most of the regulatory obligations unless the National

Regulatory Authorities declared them with significant market power in their national interconnection markets. Without such a declaration or a parallel intervention, mobile operators do not have the obligation to adapt prices to costs but only not to discriminate.[573]

The action by the Commission, even if in itself it did not lead to any final decision, forced the mobile operators to reduce their termination prices, but also the NRAs to initiate investigations for the establishment of more permanent solutions. In the same way one can understand the much studied intervention of the Italian Autorità Garante della Concorrenza e del Mercato,[574] which imposed a major sanction on the two leading mobile operators in Italy for the collusive agreement co-ordinating mobile telephony prices as well as access prices to the their networks.

It has to be pointed out, though, that as it has been shown, the scope of the rules on competition is not as wide as the regulatory rules on access. As a result, the rules on competition will not always provide an efficient mechanism for governing network access in case regulation fails.

10.3. COUNTER-BALANCED RELATIONSHIPS.

10.3.1. Regulation counterbalances antitrust.

218. Denaturalisation of antitrust. The major risk derived from the application of the rules on competition to network access conflicts is, as it has

[572] See Press release IP/98/707, of 27.7.98.

[573] For an analysis of the potential anticompetitive effects in the framework of the fixed-mobile convergence see Analysys (1999): "Consumer Demand for Telecommunications Services and the Implications of the Convergence of Fixed and Mobile Networks for the Regulatory Framework for a Liberalised EU Market", Brussels.

[574] *Vide supra* Chapter 10.2.1 Regulation Complements Antitrust.

been shown, the risk of denaturalisation of such rules.[575] European competition Law has traditionally tended to adopt a regulatory role against market power. Network access issues stress this tendency, as market failures (both permanent and transitory) require not only the proscription of anticompetitive refusals to deal but also the prescription of access conditions when market mechanisms are weak or non existent. The denaturalisation of the rules on competition entails important risks, as the solutions for network access conflicts could be expanded to other situations of market power based in market driven evolution due to the efficiency produced by legitimate competitive advantages.

The very same existence of the ONP regulatory framework reduces the risk of denaturalisation. The introduction of specific regulatory mechanisms for the solution of the access conflicts eliminates the pressure on competition authorities to over-stretch their competencies in order to provide solutions to the existing conflicts. As the regulatory framework provides more efficient mechanisms for the protection of the general interest, earlier regulatory intervention excludes in most of the cases the intervention of the competition authorities.

The risk of denaturalisation is not completely eliminated, though, as competition authorities might still be tempted to over-stretch the rules they are charged with applying in order to expand the reach of their competencies against the regulatory authorities or in order to provide solutions to conflicts unresolved by the regulatory authorities. Nevertheless, the more efficient the regulatory intervention, the smaller the room to manoeuvre left to competition authorities will be. As a result, efficient intervention is incentived.

Particularly risky is the early elimination of the existing regulatory framework on network access, as well as the lack of regulatory obligations on operators of new electronic communications networks which do not suffer the

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[575] *Vide supra* Chapter 8.3 The Adoption of the Essential Facilities Doctrine in Europe.

pressures of effective competition. In case there is no regulatory framework nor effective competition due to the existence of a market failure, the rules on competition will be denaturalised in order to face the demand for public intervention.

10.3.2. Antitrust counter-balances regulation.

219. Over-regulation. Regulation offers flexible mechanisms for public intervention. Such flexibility, nevertheless, entails the risk of over-stretching the use of such mechanisms by public authorities in order to ensure the active presence of the State in the liberalised markets even if the market failure which generated the need to intervene disappeared over the time. The phenomenon of over-regulation has been too common in the telecommunications sector,[576] and has not disappeared after liberalisation. As a matter of fact, the 99 Review of the Community regulatory framework is aimed to a great extent at preventing the cases of over-regulation detected in some Member States.[577]

The regulatory framework on network access contains various references to the elimination of the superfluous regulation.[578] Nevertheless, it is for the National Regulatory Authorities to decide whether to eliminate their intervention. It seems evident that the regulatory authorities are not the better suited to evaluate the need for their intervention.

The rules on competition apply initially to undertakings active in the market and not to public authorities. Nevertheless, different mechanisms have evolved which allow the Community competition authorities to evaluate and

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[576] *Vide supra* Chapter 2.4.2. The Regulated Monopoly (1921-2000).

[577] The proposal to reduce the intervention as regards access to the market through the elimination of the Individual License category can only be understood as a reaction against the excesses in some Member States where as France, Italy or Spain where complex schemes have been introduced in order to maintain certain public control over the operators.

[578] *Vide supra* Chapter 9.1. General Principles.

obstruct the anticompetitive effects of public measures. As a result, such mechanisms are at the disposal of the Commission to counter-balance the tendency to over-regulation. The application of Article 82 EC Treaty, through the *effet util* doctrine, as well as Article 86 EC Treaty, allows the Commission to initiate procedures against Member States in order to obstruct public measures with anticompetitive effects. The Commission has announced its intention to apply such mechanisms in case NRA regulate on network access with anticompetitive effects.

220. Access Notice. The Access Notice clearly states that "under Community Law, national authorities, including regulatory authorities and competition authorities, have a duty not to approve any practice or agreement contrary to Community competition Law".[579] Furthermore, "the NRAs must ensure that actions taken by them are consistent with community competition Law. This duty requires them to refrain from action that would undermine the effective protection of Community law rights under competition rules. If the national authorities act so as to undermine those rights, the Member State may itself be liable for damages to those harmed by its action".[580]

The Access Notice refers to the competition Law mechanisms in the hands of the Commission against anticompetitive practices by the NRAs: "if a National Regulatory Authority were to require terms which are contrary to the competition rules, [...] the member State itself would be in breach of Article 3(g) and Article 5 [now Article 10] of the Treaty and therefore, subject to challenge by the Commission under Article 169 [now Article 226]. Additionally, if an undertaking were required or authorised by a national regulator to engage in behaviour constituting an abuse of its dominant position, the member State would also be in breach of Article 90(1) [now article 86(1)],

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[579] *Vide* Access Notice, para. 13 (*supra* footnote 562).

[580] *Vide* Access Notice, para. 19 (*supra* footnote 562).

and the Commission could adopt a decision requiring the termination of the infringement".[581]

221. Article 86. Article 86(1) EC Treaty[582] is addressed to the Member States and requires them not to adopt any measure contrary to the Treaty rules, and in particular to the rules on competition, in favour of public undertakings or undertakings with special or exclusive rights.[583] Article 86 not only confirms the applicability of the rules on competition to public undertakings, but it also provides a procedure for the Commission to declare the incompatibility of a state measure with the rules on competition, through a Decision or even through a Directive.

Article 86 EC Treaty outlaws public intervention in support of anticompetitive behaviours of a public undertaking. Such support can take the form of a mere assistance for the infringement, or it can encourage the anticompetitive behaviour or it can even impose it on the undertaking.

More frequent has been the Commission intervention against State measures contrary to Article 86 in relation to Article 82, as the public nature of the special or exclusive right often ensured a dominant position to the undertaking and the possibility of abusing that position. Particularly interesting are the measures related to discriminatory treatment,[584] illegitimate extension of

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[581] *Vide* Access Notice, para. 61 (*supra* footnote 562).

[582] "In the case of public undertakings and undertakings to which Member States grant special or exclusive rights, member States shall neither enact nor maintain in force any measure contrary to the rules contained in this Treaty, in particular to those rules provided for in Article 6 and Articles 85 to 94".

[583] For an evaluation of Article 90 see BLUM and LOGUE (1997): "*State Monopolies under EC Law*", Wiley, Chichester; BRIGHT, C. (1993): "Article 90, economic policy and the duties of member states", in *European Competition Law Review*, vol. 14, no. 6, pp. 263-272; GARDNER, A. (1995): "The Velvet Revolution: Article 90 and the triumph of the Free Market in Europe's Regulated Sectors", in *European Competition Law Review*, vol. 16, no. 2, pp 78-86; RODRIGUES, S. (1995): "Comment intégrer les principes du service public dans le droit positif communautaire: quelques propositions", in *Revue Française de Droit Administratif*, no. 2, pp. 335-342.

[584] "A system of undistorted competition, as laid down in the Treaty, can be guaranteed only if equallity of opportunity is secured as between the various economic operators", C-202/88, *France v.*

a dominant position,[585] cross-subsidies,[586] and inability to meet demand.[587] Nevertheless, intervention is also possible with regard to the infraction of Article 86 in relation to Article 81, in cases where public undertakings were engaged in collusive agreements.[588]

In such a way, regulatory intervention affecting the telecom operators controlled by public authorities (and it is the case of some of the leading operators in Europe, such as France Telecom and Deutsche Telekom), as well as those operators which still enjoy exclusive or special rights (for instance the case of Telefónica, which has an special right for the provision of cable television services), are bound to the scrutiny of the Commission, which can adopt a Decision or a Directive in order to obstruct the anticompetitive measure.

222. ***Effet util.*** The EC Treaty does not contain a parallel provision to Article 86 imposing on Member States the obligation not to adopt anticompetitive measures in favour of private undertakings without exclusive or special rights. Nevertheless, the ECJ and the Commission have developed the *effet util* doctrine[589] that imposes a similar obligation. Member States contravene the general obligation not to obstruct the fulfilment of the objectives defined in the EC Treaty defined in Article 10(2) EC Treaty if they adopt measures which obstruct the effectiveness of Articles 3(g), 81 and 82, which contain the rules on competition. As a result, the Commission can initiate an infringement procedure (Article 226 EC Treaty).

Commission, [1991] ECR I-1223, para 51; and Commission Decision of 18 December 1996, GSM Spain, OJ 1997 L 76/19, para. 19.

[585] See C-18/88 *RTT v. GB*, [1991] ECR I-5941.

[586] SeeT-77/95, *French delivery services*, [1997] ECR II-1.

[587] See C-41/90, *Höfner*, [1991] ECR I-1979.

[588] This was the case in C-393/92, *Almelo*, [1994] ECR 1477, and Commission Decision of 16 january 1991, *IJsselcentrale*, OJ 1991 L28/32.

As it was stated by the ECJ: "[...] Member States may not enact measures enabling private undertakings to escape from the constraints imposed by articles 85 to 94 of the Treaty. At all events, Article 86 [now art. 82] prohibits any abuse by one or more undertakings of a dominant position, even if such abuse is encouraged by a national legislative provision. In any case, a national measure which has the effect of facilitating the abuse of a dominant position capable of affecting trade between member states will generally be incompatible with articles 30 and 34, which prohibit quantitative restrictions on imports and exports and all measures having equivalent effect .[590]

The application of the *effet util* doctrine in relation to Article 82 EC Treaty has not been common. This is not difficult to understand, as it has been usually the case that dominant undertakings benefiting from public support for the abuse of their position were public undertakings or undertakings with special or exclusive rights. In such cases Article 86 EC Treaty provides a more efficient procedure. Nevertheless, some precedents exist, as the very same *Inno v. ATAB*.

On the contrary, the application of the *effet util* doctrine in relation to Article 81 EC Treaty has been more common. The ECJ, through its extensive case law, has made clear that public administrations cannot impose, reinforce, extend or favour collusive agreements,[591] nor delegate public functions to private operators which allow them to reach the same scope as with a collusive agreement.[592]

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[589] See GYSELEN, L. (1989): "State action and the effectiveness of the EEC Treaty's competition provisions", in *Common Market Law Review*, vol. 26, pp. 33-60; VICIANO, J. (1995): "*Libre competencia e intervención pública en la economía*", Tirant lo Blanch, Valencia.

[590] C-13/77, *Inno v. ATAB*, [1977] ECR 2115, para 33-35.

[591] See C-229/83, *Au ble vert*, [1985] ECR 1; C-231/83 *Cullet v. Leclerc*, [1985] ECR 305; C-123/85, *BNIC v. Clair*, [1985] ECR 391; and C-254/87, *L'aigle distribution*, [1988] ECR 4457.

[592] See C-267/86, *Van Eycke v. ASPA*, [1988] ECR 4769.

The obligation imposed on Member States to ensure the effectiveness of the rules on competition contained in the EC Treaty is also applicable to the National Regulatory Authorities. The NRAs measures impose, reinforce, extend or favour anticompetitve behaviours by the telecommunications operators can, therefore, be subject of an Article 226 infringement procedure.

223. Article 82. Both Article 86 and the *effet util* doctrine provide the legal basis for the Commission intervention against measures adopted by the National Regulatory Authorities in relation to network access which might be contrary to the effectiveness of Article 82 EC Treaty. A tendency for some NRAs to protect the national champion, the former monopolist, against competition by foreign operators installed in a Member State, can be identified. Often, the protection of the incumbent's interests ensure a better price in the privatisation and, therefore, a direct economic benefit for public authorities. In many instances such intervention will also be contrary to Article 30 and 59 of the EC Treaty.[593]

The universal service scheme implemented by the NRAs is prone to conflict. Universal service has traditionally been the burden that legitimated the existence of the exclusive rights. After the de-monopolisation, universal service might legitimate discriminatory measures for the benefit of the incumbent. Even if initially it might seem that universal service is a burden, it might not be so if regulatory authorities ensure a sufficient level of finance by competitors. At the same time, the provision of universal service provides certain benefits such as the obtention of economies of scale, brand recognition ubiquity etc.

The automatic appointment of the incumbent as the operator in charge of the universal provision of the basic services[594] might not be justified when new

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[593] *Vide supra* MARTÍNEZ LAGE and BROKELMANN (footnote 570) for the conflicts on digital satellite television.

[594] *Vide supra* Chapter 9.1. General Principles.

comers reach a certain point of maturity and are in the position to provide such services. At the same time, the provision of an excessive burden of new comers for the financing of the service[595] might obstruct their development at the same time that it might provide an exaggerated income to the operator in charge of the provision of the services. In such cases, Article 82 EC Treaty in relation to Article 86 or to Articles 5(2) and 3(g), could be breached as a state measure would distort the necessary equality of opportunity for all the operators. As a result, the incumbent dominant position would be strengthened.[596] As a matter of fact, the Commission initiated a procedure against the French Republic for the excessive burden imposed by the universal service scheme.

The definition by NRAs of network access condition for bilateral contracts between operators might also breach Article 82. The different regulatory mechanisms in the hands of the NRAs allow them to determine important elements of network access contracts such as price and technical conditions, particularly in case of lack of agreement between the operators.[597] The conditions defined by the NRA might benefit the dominant operator, as they might impose, reinforce, extend or favour abusive behaviours of the operator as exclusionary practices which would strengthen the dominant position and therefore obstruct the technical evolution and the future quality and price of the telecommunications services. For instance, access prices could be fixed at a very high level and they could be combined with poor technical conditions which would ensure the incumbent the control over the whole management of the process (location of the interconnection points, for instance). Such measures could be challenged in front of the Commission, as they would be contrary to the effectiveness of Article 82 in relation to Article 86 or Article 5(2) and 3(g).

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[595] *Ibid.* for the French case.

[596] *Vide* Commission Decision GSM Spain, p. 26 (*supra* footnote 584).

224. Article 81. Equally interesting are the State measures potentially incompatible with Article 81 EC Treaty. Liberalisation should lead to the gradual disparition of the dominant positions in the telecom markets. Nevertheless, regulatory authorities could be tempted to extend the application of the regulatory framework on network access. Such intervention could entail anticompetitive effects as it might foster collusive agreements between the operators.

On the one hand, public intervention on network access might foster collusive agreements between the incumbent and the category of new comers which has appeared following the traditional structure of the telecom operators, in order to obstruct more aggressive competitors.

Many of the new comers share with the incumbent a common network architecture and a very similar market philosophy. On the contrary, there are other operators, usually smaller, which are following different models for the provision of the service. These operators might use a different technology (wireless local access or IP technologies, for instance) or more aggressive pricing based on access to the most efficient network elements at each segment, or simply are centred on the most profitable niche markets.

New comers which are rather following the incumbent philosophy and building comprehensive networks with similar technologies might succeed in making profits in some niche markets but it seems to be the case that they do not seriously menace the position of the incumbent in the overall telecommunications market. The aggressive operators, on the contrary, are a serious menace, even if potential, for the incumbent, as the aggressive technological options might provide a decisive competitive advantage in the future. At the same time, they are a menace for the rest of new comers, as their

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[597] *Vide supra* Chapter 9.2.3 Compulsory Access.

competitiveness might ensure them the control of the most profitable niche markets.

As a consequence, there is a common interest for the incumbent and the more conventional new comers to introduce barriers to the more aggressive new comers. Such barriers can be introduced in the access contracts, and can be protected by the regulatory authorities. The similar structure of the networks ensures a simpler interconnection of the incumbents and the conventional new comers. The application of the same conditions to the more aggressive new comers might obstruct them, as they might be forced to adapt their more sophisticated networks to the traditional structure of the incumbent's network. In this way, the competitive advantage of the innovative new comer could be eliminated or at least reduced. The intervention of the NRA might confirm such access conditions or even impose them on the operators. In such a way, a public measure could strengthen or even impose the anticompetitive result of a collusive agreement among a certain category of operators against their competitors.

Furthermore, public intervention could even foster more open discriminations against certain categories of new comers. This might be the case in certain Member States where access can be granted for different prices according to the nature of the operator requiring it. In Spain, following the French example, price differences of 30% on interconnection of Type B and Type A operators with Telefónica were approved by the public authorities as foreseen in the legislation.[598] As a result, Type B operators, those ready to accept the access network conditions of the regulatory authorities, benefit against those competitors with more heterodox strategies. Such a discrimination might be contrary to the rules on competition, not only because

[598] See MONTERO, J. J. (1999): "¿Salvaguardia de la competencia o de los competidores? Otra visión de la política española de telecomunicaciones", in *Revista de Derecho de las Telecomunicaciones e Industrias en Red*, vol 5, pp. 145-162.

it might benefit the incumbent and therefore protect its dominant position while existing, but also might be contrary to Article 81 in relation with Articles 86 or 5(2) and 3(g), as they might impose the same result as a collusive agreement between Type B operators against Type A operators. As a matter of fact, the Commission in the Access Notice has put forward the view that such discriminations could amount to an anticompetitive behaviour contrary to Article 82 EC Treaty.[599]

On the other hand, another type of collusive behaviour could be fostered by the regulatory authorities. The imposition of extremely low access prices to the incumbent could provide the same effects as a collusive agreement among the new comers in order to impose prices on the incumbent. This could be particularly the case at the moment the incumbent loses its dominance of the market but the regulatory authorities still impose asymmetric access obligations on the former monopoly. Such an example of over-regulation could be obstructed by the Community competition authorities as it would amount to a collusion between the new comers backed or even imposed by the regulatory authorities. Such a situation would harm consumers as it would foster the permanence in the market of no efficient operators subsidised by the incumbent that would not be in the position to lower its rates for the benefit of consumers.

225. Other mechanisms. The rules on competition are not the only mechanism in the hands of the Community authorities which enable them to block the adoption of anticompetitive measures by the NRAs. Certain measures can be obstructed by the Commission through Article 226 infringement procedures based on the incompatibility of the measures with the Telecommunications Directives. An Article 226 infringement procedure could be the more efficient mechanism for the Commission to block discriminatory

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[599] *Vide supra* Chapter 9.2.3. Compulsory Access, and Access Notice, para. 123-125 (*supra* footnote 562).

access conditions such as the one studied in Spain, as paragraph 5(1) of Directive 97/33/EC states that such differences should never distort competition.[600]

At the same time, the regulatory framework on network access contains certain provisions that grant power to the Commission to obstruct the regulatory intervention of the NRAs. This is the case for instance, of the provision which allows the Commission to request NRAs to justify the classification of certain operators as having or not having significant market power.[601] In this way, the classification which allows the asymmetric distribution of obligations is subject to the scrutiny of a different institution.

10.4. CONCLUSIONS.

226. Final. Throughout this thesis it has been argued that the rules on competition and the regulatory framework not only do not necessarily conflict with each other, but beneficial effects can be derived from their co-ordination. Network access, the most delicate issue in the liberalised telecommunications markets, can be better approached by public authorities with the right combination of both instruments. Antitrust and regulation complement each other and, at the same time counter-balance the negative tendencies of each instrument when dealing with access issues.

The regulatory framework on access developed by the Community institutions and implemented by the Member States complements the competition rules of abuse of dominant position, and in particular the refusal to deal and the essential facilities doctrines. The regulatory framework is the best-

[600] *Vide supra* Chapter 9.2.3. Compulsory Access.

[601] See Article 25(2) of Directive 98/10/EC and Article 18(2) of Directive 97/33/EC.

suited instrument to substitute the constraints of competition which lack due to different market failures and ensure the satisfaction of the general interest objectives. At the same time, the rules on competition complement the regulatory framework, as they provide a safety network for those cases in which, for a variety of reasons (loopholes, capture etc.), the regulatory framework does not provide an efficient solution against an anticompetitive refusal to grant access.

If both instruments complement each other, they also counterbalance themselves. The very same existence of the regulatory framework on network access eliminates the need for the competition rules to be stretched and denaturalised in order to provide mechanisms for public intervention on the matter. At the same time, the rules on competition counter-balance some of the excesses of the regulatory intervention, the leading mechanism of intervention in the period of transition to full competition in the market.

The rules on competition, and in particular Article 86 and Articles 5(2) in relation to Article 3(g), allow to impose controls on the measures adopted by the national regulatory authorities. Nevertheless, such control is limited, as it is only effective with regard to the anticompetitive effects of the regulatory intervention. Furthermore, the rules on competition are very strictly defined, particularly with regard to their indirect application to state measures.

As a result, the rules on competition counter-balance the most clear examples of anticompetitive state intervention, but do not ensure the elimination of all the distortions of the market without a legitimate justification.

The most efficient counter-balance mechanisms are the ones created by the very same regulatory framework but bestowed not to the regulatory authorities but to different entities and in particular to the Commission. The Commission is particularly well suited to review the validity of the regulatory intervention. As a competition authority it has the know-how to evaluate

markets and the effects on such markets of State measures. At the same time, the Commission constitutes a different layer of intervention, and as a result, is usually outside of the reach of some of the forces that could capture a National Regulatory Authority.

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