

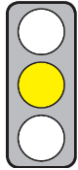
BROADBAND INVESTMENT: NON-DISCRIMINATION, PRICE CONTROL AND COST ACCOUNTING

cepPolicyBrief No. 2014-33

KEY ISSUES

Objective of the Recommendation: The Commission wants to promote investment in the next generation of telecommunications networks (NGA networks) and maintain effective competition.

Affected parties: Operators of telecommunications networks and providers of broadband services.



Pro: (1) The EoI approach is suitable for avoiding distortions of competition. In view of diverging national market conditions, the decision on whether the EoI approach is proportionate should be left up to the national regulatory authorities (NRAs).

(2) The ability of NRAs to remove price controls increases scope for stimulating sluggish demand for fast broadband services by way of a dynamic pricing policy. This may promote investment in NGA networks.

Contra: (1) NRAs should not only remove price controls but also access controls where "effective competition" by way of alternative infrastructures is possible.

(2) Establishing an EU-wide standard costing methodology (BU LRIC+) whilst simultaneously pre-empting the results of its use, casts doubt on NRA independence which is mandatory under EU law.

CONTENT

Title

Recommendation (2013/466/EU) of 11 September 2013 on **consistent non-discrimination obligations and costing methodologies** to promote competition and enhance the broadband investment environment

Brief Summary

► Context and objectives

- In order to maintain a level playing field, the national regulatory authorities ("NRAs") can prescribe rules for operators of telecommunications networks with significant market power (SMP operator), relating to access by other companies ("external service providers") to its networks ("remedies"). These include, in particular, the following obligations:
 - "Non-discrimination": An SMP operator must allow external service providers access to its networks on terms and conditions which are "equivalent" to those applicable to internal providers within its own undertaking [Art. 10 Access Directive (2002/19/EC)].
 - "Price control": An SMP operator must provide external service providers with wholesale products - particularly network access - at controlled prices (Art. 13 Access Directive).
 - "Cost accounting": In order to calculate controlled wholesale prices, an SMP operator must fulfil the obligations attached to the cost accounting system to be used (Art. 13 Access Directive).
- The scope of the Recommendation is limited to remedies relating to the following network access products (Recital 5):
 - passive network access, that is, in particular, unbundled access to local lines [generally a copper local-loop infrastructure (copper LL, Market 4 of the recommendation on relevant markets (2007/879/EC)] or a virtual access product (generally with high optic-fibre content) and
 - active network access, in particular bitstream access to the existing wholesale product [Market 5 of the recommendation on relevant markets (2007/879/EC)].
- According to the Commission, there are "significant" inconsistencies between the remedies imposed by the NRAs although the "underlying market problems are comparable". These differences "hold back the development of the internal market". (Recitals 6 to 8)
- By way of the Recommendation, the Commission wants to promote investment in next generation access networks (hereinafter: NGA networks) and at the same time maintain effective competition on the broadband market (Recital 3). This will take place by
 - strict non-discrimination obligations,
 - greater clarity as to when the obligations on price control for NGA networks should cease and
 - a consistent costing methodology.

► **Non-discrimination by Equivalence of Input (Eol) and technical replicability**

- As regards remedies for non-discrimination, two approaches are possible (Para. 6 (g) and (h)):
 - "Eol" (Equivalence of Input): The SMP operator must allow external and internal service providers to have network access on "the same" terms and conditions and using "the same" systems and processes.
 - "EoO" (Equivalence of Output): The SMP operator must allow external and internal service providers to have network access on "comparable" terms and conditions and can use "different" systems and processes for this.
- The NRA will first carry out a "proportionality assessment" to find out whether Eol should be used. The decisive factor in this regard is whether the competition benefits of Eol outweigh the costs of compliance for the SMP operator. (Para. 7)
- When carrying out the proportionality assessment, the NRA will take account of the fact that (Para. 7)
 - compliance costs for NGA networks are often lower than for the existing copper networks,
 - where Eol is used, price control may not be needed (see below),
 - Eol may have a "potentially positive" effect on competition and innovation and
 - the SMP operator may have already committed to Eol voluntarily.
- Where Eol is disproportionate, NRAs should opt for EoO (Para. 9).
- An SMP operator, upon which the NRA imposes a non-discrimination obligation, must allow external service providers to have network access to the extent that they can "technically replicate" the operator's new retail products, i.e. can offer them in a comparable form. This applies, in particular, where Eol has not yet been fully implemented. (Para. 11)
- The NRA or the SMP operator tests the technical replicability. Where the NRA conducts the test, it must require the SMP operator to provide details of the new retail products "with sufficient notice" prior to their launch. Where the operator itself conducts the test, the NRA should "validate" the test results. (Para. 14 to 16)
- The NRA should oblige the SMP operator to (Para. 17 and 18)
 - amend the network access product in a way that ensures its technical replicability and
 - cease or delay provision of the retail product pending compliance with the requirement of technical replicability.

► **Removal of price controls for access to NGA network**

- The NRA should not control the prices of the NGA network access products of an SMP operator if the latter is subject to (Para. 48 and 49)
 - a non-discrimination obligation consistent with Eol,
 - obligations relating to technical replicability of retail products if Eol has not been fully implemented, and
 - obligations relating to the economic replicability of its retail products; the requirement for this is that its retail price exceeds the network access tariff which it imposes to the extent that its common costs and downstream costs are covered.
- An additional requirement for the removal of price controls is, (Para. 48 and 49)
 - in the case of active NGA access products, that a competitor be provided with sufficient upstream and regulated passive (or similarly functioning active) access products, or that alternative infrastructures are available which create a demonstrable retail price constraint,
 - in the case of passive NGA access products, that the SMP operator offers copper access at cost-oriented, controlled prices ("price anchor"), or there are alternative infrastructures that exercise a "demonstrable retail price constraint".
- The NRA can also remove price controls on NGA access products where there is "effective equivalence" of access and "effective infrastructure-based competition" (Para. 58).
- Following the removal of price controls, the NRA can reintroduce them or impose penalties if the SMP operator fails to fully implement an agreed Eol (Para. 54).
- Along with the removal of price controls, the NRA should (Para. 55)
 - monitor the investment and competitive environment for NGA networks and
 - obtain information from the network operators about their NGA roll-out plans.
- The NRA should differentiate its regulatory practice within geographical markets and also remove price controls in areas where the said conditions have been fulfilled ("regional regulation") (Para. 50).
- An SMP operator can award volume discounts on access to its networks. Discounts for internal service providers must not, however, exceed those for external providers. (Recital 19)

► **Costing methodology "BU LRIC+"**

- When controlling the prices of the network access products of an SMP operator, the NRA should adopt the "bottom-up long-run incremental costs plus" costing methodology (BU LRIC+). This applies to both copper and NGA networks. (Para. 30)
- The BU LRIC+ methodology takes account of (Para. 31)
 - the variable costs - including investments - of a "hypothetical efficient" operator in building a modern efficient NGA network and
 - a supplement for common costs.

- When modelling the NGA network, the NRA should ensure that (Para. 32)
 - the NGA network does not have to consist wholly of "optical elements" - optical fibre - and
 - some existing civil engineering assets can host NGA networks but other civil engineering assets will have to be newly constructed.
- The NRAs should implement the BU LRIC+ methodology by no later than the end of 2016 (Para. 39). They can, however, continue to apply another costing methodology where this (Para. 40)
 - was already in use at the time of entry into force of the Recommendation,
 - meets the objectives of BU LRIC+ - particularly the creation of incentives for investment in NGA networks - (Recitals 25 to 28),
 - reflects the shift from a copper to an NGA network, if it is not modelling an NGA network,
 - takes into account that certain civil engineering assets will probably not be replicated and
 - guarantees stable, transparent and foreseeable copper network access prices.
- The Commission anticipates that the NRAs will impose an average monthly rental access price for the copper local loop of between € 8 and € 10 ("price band") expressed in 2012 prices (Para. 41). The NRAs are not obliged to impose access prices within this price band however (Para. 43).
- The NRA of a Member State in which the access prices for the full unbundled copper local loop fall outside the price band should recalculate the access prices on the basis of BU LRIC+ "as soon as possible" to ensure its implementation by the end of 2016. This does not apply to NRAs whose own costing methodology fulfils the aforementioned criteria. (Para. 43)
- If the NRA is unable to introduce the BU LRIC+ costing methodology by the end of 2016, it should set "interim access prices" based on rates in "comparable countries" (Para. 45).

Policy Context

The Recommendation is derived from the objectives established in 2010 in the "Digital Agenda for Europe (DAE)" [Communication COM(2010) 245, see [cepPolicyBrief](#)], in which the roll-out of next generation broadband access networks (NGA networks) plays an important role. In parallel to the Recommendation, the Commission has submitted a Regulation on measures concerning the European single market for electronic communications and to achieve a Connected Continent [COM (2013) 627] (see [cepPolicyBrief](#) on net neutrality and harmonisation of the rights of the end user, [cepPolicyBrief](#) on the notification requirements for telecommunications companies, radio spectrum and virtual broadband access products and [cepPolicyBrief](#) on roaming).

Options for Influencing the Political Process

Leading Directorate General: DG Communication

ASSESSMENT

Economic Impact Assessment

Focussing on EoI, when imposing a non-discrimination obligation, is basically correct because, by comparison with EoO, **EoI is more suitable for avoiding distortions of competition** between external and internal service providers, and for ensuring their equal treatment. The key factor, however, - as the Commission recommends - is to ensure that its implementation is proportionate because, in practice, EoI is routinely too complex or expensive and is often unpopular even with external service providers. **In view of the diverging national market conditions, it is appropriate for the assessment criteria recommended by the Commission to be non-binding and the decision as to which approach to use to be left up to the national regulatory authority (NRA).**

The ability of the NRA to remove price controls, subject to sufficient protective measures - non-discrimination, technical and economic replicability -, **may promote investment in NGA networks because it increases the scope**, for both the SMP operator and external service providers, **to stimulate sluggish demand for fast broadband services by way of a dynamic pricing policy.** The recommendation does not go far enough however. **The NRAs should not only remove price controls but also access obligations where "effective competition" by way of alternative infrastructures is possible.**

The call to the NRAs to differentiate regulation on a regional basis is promising because the shift from copper to NGA networks will break up the traditional market structures in many places. Instead of the national monopolistic structure, which has been usual up to now, some regions may have several SMP operators, others only one. In this situation, it makes sense to define markets on a regional basis and remove price controls in those areas with effective competition (see also [cepStudy](#)).

Establishing an EU-standard costing methodology (BU LRIC+) whilst simultaneously implicitly pre-empting the results of its use - € 8 to € 10 for the copper local loop - **is highly questionable.** Although this is officially a non-binding recommendation, in practice there is pressure to comply with it because NRAs are legally obliged to take the "utmost" account of the Commission's recommendations and to justify any divergences (Art. 19 (2) Framework Directive). **Thus the Commission casts doubt on NRA independence, which is mandatory under EU law** (Art. 3 Framework Directive).

The question is whether the impartial use of BU LRIC+ by the NRAs would in fact steer the network access prices for copper local loop, which until now have varied widely, in the direction desired by the Commission [Impact Assessment SWD(2013) 329, p. 56]. National differences, such as population density, geography and the cost of wages and materials, continue to exist and if an NRA establishes a price in the desired range, it will be unclear whether this is driven by objective economic reasons or political considerations. The situation is made more difficult by the fact that, in establishing a price range, the Commission is misusing the NRA's power to set prices, for a political objective - the roll-out of fast NGA networks - thus undermining the actual objective of achieving price control based on market conditions. The lack of investment is not primarily the result of varying network access prices in the Member States but is in fact due to technical factors and can be partly explained by the sluggish demand for fast broadband services on the part of the end-customer.

Legal Assessment

Legislative Competency

The Commission can adopt the Recommendation because it is of the opinion that there are barriers to the single market resulting from divergent implementation by the NRAs of the regulatory functions provided for under the Framework Directive (2002/21/EC) and the individual telecommunications Directives (Art. 19 (1) Framework Directive).

Subsidiarity

The Recommendation is in breach of the principle of subsidiarity. This allows EU action only in cases where the Commission's objectives cannot be adequately achieved at the Member State level but are better achieved at EU level. The Commission recommends that the NRAs consider a specific course of action in relation to the imposition of remedies on the local loop and bitstream access market. Although the range of possible remedies is rightly harmonised EU-wide, each Member State represents (at least) one geographically defined local loop and bitstream market. The choice of which actual remedy to use is therefore best made at national level. For the same reason, the objective of promoting investment in NGA networks can also be better achieved at national level.

Proportionality with Respect to Member States

The Recommendation is proportionate because Recommendations are basically non-binding (Art. 288 (5) TFEU). Under Art 19 (1) Framework Directive, the NRAs must take the "utmost" account of recommendations in carrying out their functions (Art. 19 (2), sub-paragraph 2, sentence 1 Framework Directive). In practice, however, most NRAs do follow these recommendations. An NRA can, however, decide not to follow a recommendation. It must then inform the Commission of its decision and give reasons for its position (Art. 19 (2), sub-paragraph 2, sentence 2 Framework Directive). Under Art. 19 (3) Framework Directive, the Commission cannot transform this Recommendation into a binding decision as it does not relate either to market definition or analysis (see [cepStudy](#)).

Compatibility with EU Law in other Respects

Where an operator has a powerful position on a specific market, the NRA must impose one of the remedies which are set out in the Access Directive (2002/19/EC) (Art. 8 (2) Access Directive). However, the NRA has considerable scope for discretion in choosing the actual measure (Art. 8 (4), sentence 1 Access Directive). Although the Recommendation advises the NRAs on which remedy to use in certain situations, since it is non-binding - in strictly legal terms - the discretionary power of the NRAs remains in place.

Impact on German Law

Application of the BU LRIC+ costing methodology by the German Federal Network Agency (BNetzA) is possible. Since 2012, the BNetzA has been able to set prices using methods other than the principle of the "costs of efficient service provision". It may do so when this is more suitable for achieving the regulatory objectives under Section 2 Telecommunications Act (TKG). The superior suitability must be specifically substantiated. (Section 31 (2), sentence 1 No. 2 TKG)

Conclusion

The EoI approach is suitable for avoiding distortions of competition. In view of diverging national market conditions, the decision on whether the EoI approach is proportionate should be left up to the national regulatory bodies (NRAs). The ability of NRAs to remove price controls increases scope for stimulating sluggish demand for fast broadband services by way of a dynamic pricing policy. This may promote investment in NGA networks. NRAs should also remove access controls where "effective competition" by way of alternative infrastructures is possible. Establishing an EU-standard costing methodology (BU LRIC+) whilst simultaneously pre-empting the results of its use, casts doubt on NRA independence which is mandatory under EU law. The Recommendation is in breach of the principle of subsidiarity.