EU Consultation

ACCESS PRICES AND NGA ROLL-OUT

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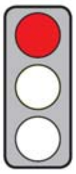
Centrum für Europäische Politik

MAIN ISSUES

Objective of the Consultation: The Commission presents its ideas on how changes in wholesale copper access prices may encourage investments in NGA Networks. These changes may be brought about by a recommendation and finally a binding decision by the Commission on costing methodologies for wholesale access prices.

Parties affected: Operators of telecommunication networks and their wholesale and end customers, investors



Pros: –

Cons: (1) The Commission intends to intervene heavily in markets, in order to achieve unrealistic political aims.

(2) There is no sound economic reason for harmonising wholesale access prices in the EU. The Commission's idea of employing "glide paths" for costing methodologies unnecessarily introduces an element of politics into regulated prices.

(3) Not politics but market forces should decide the pace of investment and the technological form of (ultra-) fast networks in the EU.

(4) It is highly contentious whether the Commission would have the competence to adopt a legally binding decision on the harmonisation of costing methodologies for wholesale access prices, especially given that such a decision implies changes that do not lie within the category of "non-essential" elements.

CONTENT

Title

Public consultation on **costing methodologies for key wholesale access prices in electronic communications** [without number] of 3 October 2011

Brief Summary

- **Objective**
  - The EU-Commission initiates a consultation aiming at issuing (at first) a non-binding recommendation. This recommendation is to guide national regulatory authorities as to "how to set wholesale access prices in the transition period from copper to fibre-based networks".
  - The Commission stresses that it has the "power" to convert this non-binding recommendation into a legally binding decision two years after adopting the recommendation. Such a decision may lead to a "harmonised application of the provisions of the (telecommunications) framework, including the remedies imposed".
- **Background**
  - The Commission criticises the fact that the different approaches of national regulatory authorities to setting access prices result in different prices for copper access across the EU. According to the Commission, this leads to a lack of legal certainty and predictability, which hampers investments and hence competition.
  - The Commission identifies difficulties for alternative operators based on copper to compete with cable platforms or mobile operators (LTE) on the basis of current copper access prices.
  - The Commission is dissatisfied with the limited roll-out of (ultra) fast NGA-Networks in the EU. It identifies two measures to remedy this. Firstly, the considerable risks associated with investments in these networks should be "duly remunerated". Secondly, it argues that relative prices for wholesale access services for copper can significantly affect the incentives to invest in NGA-Networks.
- **Calculating access-costs with different models**
  - The Commission acknowledges that in calculating regulated access prices, national regulators use a variety of cost models. These vary from fully distributed costs (FDC) to long-run incremental costs (LRIC) and can be combined with a bottom-up or top-down modelling approach, or a combination of both. Within these approaches, assets can be valuated using historical (at time of construction) or current costs.
  - In regulating markets 4 (wholesale fixed network access) and 5 (wholesale broadband access), about half of the national regulators apply a bottom-up, long-run incremental cost approach combined with a valuation at current costs (CCA BU-LRIC).
  - The Commission argues that the possibility of this CCA BU-LRIC leading to an "overcompensation" for access-prices to copper networks cannot be ruled out.
  - The Commission sees reasons for considering historical costs for non-replicable assets and current costs for replicable ones. It sees ducts as non-replicable and copper (where fibre is planned) as replicable.

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- **Fostering NGA investments through relative access prices**
  - The Commission raises the question of how an increase or decrease in access prices for copper will affect investments in NGA networks. According to the Commission,
    - incumbents argue that high copper access prices generate means necessary for fibre investments, and
    - competitors argue that high copper access prices lead to "supernormal profits", which make risky investments in fibre unattractive.
  - The Commission would like to receive feedback on the idea of a glide path model, in which
    - access prices for copper – which are the result of the application by national regulators of costing models – are reduced only "after a certain time" (glide path),
    - such access price reductions for copper only take effect if previously announced fibre investments do not take place,
    - failing to invest in fibre networks is penalised with even lower copper access prices (down to short term incremental costs).
  - The Commission considers it useful to raise copper access prices in areas in which NGA investments are carried out. Prices could be raised to reach the level of the access costs of fibre.
- **Fostering NGA investments by switching off copper networks**
  The Commission raises the question of
  - whether the parallel existence of copper and fibre networks lowers the willingness to invest in fibre,
  - how, in which areas and how fast a copper switch-off would be "appropriate",
  - how to deal with customers who – also after migration to fibre – still demand narrowband services and whether a price increase for these customers would be reasonable.
- **Other questions**
  The Commission raises the question of
  - whether a technical migration from copper to fibre is absolutely necessary in order to achieve the broadband penetration aim of the Digital Agenda,
  - how the price add-on for access to new fibre networks can be calculated so as to encourage investment risks in fibre,
  - what would be the consequences of copper customers changing to cable or mobile alternatives instead of to fibre.

Statement on Subsidiarity by the Commission

The Commission does not address the issue of subsidiarity.

Policy Context

On 26 March 2010 the European Council endorsed the Strategy "Europe 2020" [COM(2010) 2020; see CEP Policy Brief] as the successor to the failed Lisbon Strategy. One of the seven flagship initiatives of the Europe 2020 Strategy is the **"Digital Agenda for Europe"** [COM(2010) 245, see CEP Policy Brief].
The "Digital Agenda for Europe" explicitly aims at speeding up **broadband penetration** in order to bring basic broadband to all Europeans by 2013. By 2020, all Europeans should have access to internet speeds of at least 30 mbps and 50% of EU households to speeds of at least 100 mbps. The Commission expects positive effects ("spill-over effects") for the overall economy from this development.
At the same time, the Commission fears that only "strong public intervention" can encourage infrastructure providers to invest in NGA networks located not only in high-density urban zones but also in less populated and profitable areas. To alleviate this problem, the Commission has developed three policy instruments:
Firstly, the Commission has developed a **state-aid** strategy to encourage NGA investments, which is based on the geographically differentiated allocation of subsidies (see: Community Guidelines for the application of state-aid rules in relation to the rapid deployment of broadband networks, CEP Policy Brief).
Secondly, in order to further promote investment in NGA networks, the European framework conditions for the deployment of NGA networks provide (both in the Framework Directive 2002/21/EC and in the NGA Recommendation 2010/572/EU) that access prices for new networks should duly take into account **investment risks**. Also, "co-investments" and "risk-sharing mechanisms" should be promoted.
Thirdly, the Commission recently proposed the **"Connecting Europe Facility"**, in which guarantees and credits issued by the European Investment Bank are to promote "project bonds" financing risky investments in new networks (see CEP Policy Brief).
The Commission's present consultation appears to introduce a new, fourth policy instrument: EU intervention in the **price regulation** of national regulators. This would not be a total novelty: the highly contested Roaming Regulation [EC No. 217/2007] has already led to the EU interfering directly in price setting. Recently, the Commission has proposed further changes to the regulation (see CEP Policy Brief).

Options for Influencing the Political Process

Leading Directorate General:	DG Information Society and Media
Consultation procedure:	The Commission accepted statements until 28 November 2011. Statements (including this one) are published at: http://ec.europa.eu/information_society/policy/ecomm/library/public_consult/cost_accounting/index_en.htm

ASSESSMENT

Economic Impact Assessment

Ordoliberal Assessment

The Commission rightly asserts that reaching one of the key aims of the "Digital Agenda for Europe", that is to provide all Europeans with internet speeds of at least 30 mbps or 100 mbps to 50% of EU-households by 2020, is becoming increasingly unrealistic, in particular due to the current pace of NGA rollout. As the consultation implies, the Commission is not willing to accept this and is therefore considering far-reaching changes to costing methodologies for wholesale access prices in an attempt to boost fibre investment. This gives considerable cause for concern.

Instead of adapting a politically set aim to economic realities, the Commission intends to expend even more effort on achieving the existing aim by influencing economic prices fixed by independent regulators. Ironically, at the same time the Commission seems to doubt whether a "technical migration from copper to fibre" is "absolutely necessary".

It is true that (regulated) prices for wholesale access products (copper) have an impact on opportunity costs (of NGA investment). Intervening in this process by "fine-tuning" costing methodologies, and hence prices, in order to reach a politically desired aim is not only incompatible with the wish (also of the Commission) for independently acting regulators. It indeed is also incompatible with a free market economy, in which prices reflect supply, demand and scarcity.

Unlike the commission seems to assume, **from an economic point of view, there is** in fact **no sound reason for harmonising access prices.** The argument that different copper access prices across Member States cause legal uncertainty and hamper NGA investment is not convincing. It seems more likely that the commission is not willing to accept the existing degree of incentives for NGA-investment connected with existing copper access prices. **Drawing attention to different prices for copper access** across Member States, **the Commission appears to be using a crutch with which to arrive at an instrument for intervention** (harmonisation procedures in Art. 19 of the Framework Directive) in order **to influence relative prices.**

The Commission needs this crutch, as the European legislator has decided not to provide it with the power to veto the remedies (copper access prices) of national regulators. After state-aid programmes, risk-add-ons in access prices and infrastructure project bonds, the Commission's intention to adopt a recommendation on costing methodologies is hence a fourth attempt to incentivise NGA investment.

In so doing, **the Commission is overreacting**. **Whether or not, how fast and to which extent the European Union actually needs (ultra) fast networks, is** not **to be decided by** bureaucrats, regulators or politicians. **Market forces** should decide whether, when and in which technological form these networks will have a place in the European IT Infrastructure.

Moreover, the Commission is focussing too much on fibre as just one of a number of technologies available for (ultra) fast internet access. **Policy measures should,** however, **be technologically neutral**. Wanting to link – as the Commission does – copper access prices to fibre investments ignores cable and mobile (LTE) as possible substitutes for such (ultra) fast access. This may cause enormous misinvestments in cases where cable or mobile make more economic sense than fibre.

Allowing for a risk-add-on for regulated access prices is a preferable policy instrument, as is does not affect the price of the technological alternative. Hence, **"glide path models" are to be rejected. They** deviate from the principle that regulated prices should reflect costs and risks. Glide path models **leave room for political wishes regarding technological changes, but this would negatively affect legal certainty and predictability and would in the medium-term negatively affect investment.**

Impact on Efficiency and Individual Freedom of Choice

Low investments in fibre and other NGA technologies cannot be explained convincingly by copper prices being "too high". A better explanation is the lack of customer demand.

Whether or not it is economically viable for one network operator to operate both a copper and a fibre network should at first be the operator's decision. An ex-ante decision by the regulator regarding an "appropriate switch-off" may unduly force operators into investments and patronises customers satisfied with copper-based services.

Equally patronising is the Commission's proposal to regionally raise copper access prices in areas with NGA investments. The aim of this exercise is clearly to drive customers out of copper, even when they see no necessity to do so. It should be noted that a regional regulation in this set-up is completely contradictory to the findings of recommendations on how to correctly regionalise regulation (see CEP-Study). According to these recommendations, the intense competition in urban areas should enable lower prices, not higher ones.

Impact on Growth and Employment

The view that the mere presence of (ultra) fast networks will boost economic growth is too simple and mechanical. Such "spill-over effects" for growth and employment are uncertain.

Impact on Europe as a Business Location

The presence of (ultra) fast networks only has a positive effect on Europe as a business location if there is a demand for services provided via these networks.

Legal Assessment

Legislative Competence

The Commission's competence to initiate consultations is beyond dispute. Equally undisputed is the Commission's competence to issue recommendations [Art. 19 (1) Framework Directive 2002/21/EC)].

It is however **highly contentious whether the Commission would have the competence to adopt a legally binding decision on the harmonisation of costing methodologies for wholesale access prices.**

Firstly, pursuant to Art. 19 (3) Framework Directive, the Commission may – with such a decision – impose a harmonised or coordinated approach only, when the "general regulatory approach" of Art. 15 and 16 (market definition and market analysis) Framework Directive has been inconsistently implemented by national regulatory authorities. Costing methodologies are the methodological basis for decisions made by national regulatory authorities regarding the exact design of regulatory remedies. However, these remedies should be seen as the logical next step of a market definition and market analysis confirming the presence of all preconditions for regulation. Hence, costing methodologies for wholesale access prices are not part of the market definition and market analysis process and can thus not be subject to a binding decision by the Commission.

Confirming this view, Art. 7 of the Framework Directive makes it clear that market definition and market analysis on the one hand and remedies on the other hand are to be seen separately. The European legislator has only granted the Commission a veto for market analyses and market definitions by national regulatory authorities. With regard to remedies, the Commission has not been granted this power. It can only apply the procedure in accordance with Art. 7a Framework Directive, according to which it may issue a non-binding recommendation to the national regulatory authorities regarding the remedy in question.

Secondly, **any decision by the Commission** pursuant to Art. 19 (3) **may only concern "non-essential elements"**. Given the fact that **costing methodologies directly affect remedies and** that the Commission has not been conferred the power to veto remedies, these elements **therefore seem highly "essential".**

Subsidiarity

Different costing methodologies amongst member states do not hamper the internal market, as long as they are designed by independent national regulatory authorities. A harmonisation of these methodologies by an agent with a political agenda might cause more distortions.

Proportionality

As yet unassessable.

Compatibility with EU Law

Unproblematic.

Possible Follow-up Actions by the EU

Following this consultation, the Commission will most likely issue a non-binding recommendation. It may, two years later, adopt a binding decision on costing methodologies, "including the remedies".

Such decisions made by the Commission in accordance with the Art. 19 Framework Directive are adopted following the "regulatory procedure with scrutiny" [Art. 19 (4), Art. 22 (3) Framework Directive in connection with Art. 5a (1) Nr. 1-4 and Art. 7 Decision 1999/468/EC (comitology)]. Although the Lisbon Treaty has replaced comitology procedures by the system of delegated legal acts and implementing acts (Art. 290; 291 TFEU), references to the comitology decision in a number of legislative acts remain valid [Art. 11 (2) Regulation (EU) Nr. 182/2011].

This means that in case of adopting such decision, the Commission is advised by a committee of national experts (COCOM) and is subject to the control of the Council and the European Parliament. The Parliament can veto the Commission's decision with a simple majority. The Council can only veto the Commission's decision with a qualified majority.

Alternative Action

Economic reasons speak against harmonising costing methodologies; legal reasons speak against the Commission making a binding decision regarding this topic. National regulatory authorities should ignore an possible, non-binding recommendation; Council and Parliament should veto a Commission decision.

Conclusion

The Commission's plans to harmonise costing methodologies for wholesale access prices represents an intervention into regulated access prices for copper in an attempt to boost NGA investment and to achieve the political aims of the digital agenda for Europe. In so doing, the Commission would weaken the independence of national regulatory authorities. Moreover, there is no sound economic reason for the Commission's intention. Market forces should decide as to the pace of investment and the technological form of (ultra) fast networks. The Commission's idea of employing "glide paths" unnecessarily introduces an element of politics into regulated prices. It is highly contentious whether the Commission has the competence to adopt a legally binding decision on the harmonisation of costing methodologies for wholesale access prices, especially given the fact that such a decision implies changes that do not lie within the category of "non-essential" elements.

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