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European Regulation of Mobile Termination Rates (MTR)

Unsustainable, arbitrary, assumptive and full of legal difficulties

by

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Main Points

- With the revision in December 2009 of the Telecommunications-Framework Directive (2002/21/EC), the Commission was given the power to transfer non-binding recommendations into binding decisions after a certain period of time. In the Case of Mobile Termination Rates (MTR), the Commission is able to do so since December 2011.
- There is a realistic chance that the EU-Commission will issue a legally binding decision, forcing national regulators to apply the pure LRIC approach to MTR.
- In our opinion, the pure LRIC model is unsustainable and is likely to lead to arbitrary results, which are to a high degree subject of political influence-taking. Above all, it presupposes knowledge to an extent which is simply not present.
- As the service of terminating mobile calls is a national market, we see no clear case for the EU-Commission to intervene in the regulation of MTR at all.
- It is by no means clear that the legal preconditions for a binding MTR-decision are fulfilled.
- A binding MTR-decision would be adopted in the comitology procedure, which allows for amendments of "non-essential elements of the (framework) directive". We believe the introduction of pure LRIC is a very essential change which should be made using the ordinary legislative procedure.
- A binding MTR-decision on pure LRIC would weaken the independence of national regulators. This deserves a serious debate; making the ordinary legislative procedure necessary.
- Political legitimacy for a binding decision is very weak. Upon signing the new Framework Directive, a high number of Member States (16) stated that the Commission should not attempt to use its power under Article 19 to bypass the lack of a veto right against remedies.
- By initiating an Art. 7a proceeding against the Dutch Regulator (OPTA) on 13th February 2012, the Commission exercises pressure on OPTA to come in line with the Commission's interpretation instead of with the one by the Dutch Tribunal.
- The forthcoming BEREC-opinion will be a first test of political support for the pure LRIC method amongst member states. If such support were present to a sufficient extent an OPTA does not step in line, the Commission may issue a binding decision according to Art. 19 FDR.
- CEP advises the Commission not to adopt an MTR-Decision and to return to the LRAIC approach in regulating MTR.

Kernpunkte

- Seit der Überarbeitung der Telekommunikationsrahmenrichtlinie im Jahr 2009 ist die Kommission befugt, nicht-verbindliche Empfehlungen nach einer bestimmten Zeitspanne in verbindliche Entscheidungen umzuwandeln. Im Fall der Mobilfunkterminierungsentgelte (MTR) gibt es diese Möglichkeit für die Kommission seit Dezember 2011.
- Es besteht die reelle Chance, dass die Kommission eine rechtsverbindliche Entscheidung trifft, um nationale Regulierungsbehörden bei der Festsetzung von MTR zur Anwendung des „Pure LRIC Ansatzes" zu zwingen.
- Das CEP vertritt die Meinung, dass das pure LRIC-Modell nicht nachhaltig ist und zu willkürlichen Ergebnissen führt, die zu einem hohen Grad politischer Einflussnahme ausgesetzt sind. Zudem setzt das Modell ein Ausmaß an Wissen voraus, das nicht vorhanden ist.
- Da die Anrufzustellung in Mobilfunknetzen ein nationaler Markt ist, sehen wir keinen ersichtlichen Grund für die EU-Kommission in die Regulierung der Mobilfunkterminierungsentgelte einzugreifen.
- Es ist keineswegs klar, dass die legalen Voraussetzungen für eine bindende MTR-Entscheidung gegeben sind.
- Eine verbindliche MTR-Entscheidung würde im Komitologieverfahren verabschiedet werden, welches Veränderungen der „nicht wesentlichen Bestimmungen der Rahmenrichtlinie" ermöglicht. Das CEP ist der Meinung, dass die Einführung des pure LRIC-Ansatzes eine sehr grundlegende Änderung ist, die im ordentlichen Gesetzgebungsverfahren beschlossen werden müsste.
- Eine bindende MTR-Entscheidung zum pure LRIC-Ansatz würde die Unabhängigkeit der nationalen Regulierungsbehörden einschränken. Dies bedarf einer eingehenden Debatte und betont die Relevanz des ordentlichen Gesetzgebungsverfahrens.
- Die politische Legitimität für eine bindende Kommissionsentscheidung ist sehr gering. Bei der Unterzeichnung der neuen Rahmenrichtlinie betonten 16 Mitgliedsstaaten, dass die EU-Kommission ihre neuen Kompetenzen nach Artikel 19 der Rahmenrichtlinie nicht dazu nutzen sollte um das Fehlen eines Vetorechts gegenüber Regulierungsmaßnahmen zu umgehen.
- Indem die Kommission am 13. Februar 2012 ein Art. 7a Verfahren gegen die Niederländische Regulierungsbehörde (OPTA) eingeleitet hat, übt sie Druck auf die OPTA aus, sich dem pure LRIC Ansatz der Kommission – und nicht dem Ansatz des niederländischen Gerichts – anzuschließen.
- Die ausstehende BEREC-Stellungnahme ist ein erster Test für die politische Unterstützung des pure LRIC Ansatzes durch die Mitgliedstaaten. Ist eine ausreichende Unterstützung vorhanden, und passt die OPTA ihre Regulierungsmaßnahmen nicht an, muss damit gerechnet werden, dass die Kommission eine bindende Entscheidung nach Art. 19 RRL herbeiführt.
- Das CEP empfiehlt der Kommission, keine MTR-Entscheidung zu treffen und bei der MTR-Regulierung zum LRAIC-Ansatz zurückzukehren.

Content

Main Points 1

Kernpunkte 2

I. Introduction 4

II. The EU-Commission's MTR-recommendation 2009/396/EC 5

1. Content 5
2. Possible next step: A Binding Decision according to Art. 19 FDR 6

III. An Economic Assessment of the MTR-recommendation 7

1. Need for MTR-Regulation 7
2. Regulating with the Pure LRIC Model 7
   - 2.1 Pure LRIC: what does it really mean? 7
   - 2.2 Pure LRIC: Three Arguments Against 8
3. Need for Intervention by the EU-Commission 10
4. Harmonisation and Symmetry 11

IV. A Legal Assessment 12

1. At Present: Recommendations and "comply or explain" 12
2. In the Future: Moving from a Recommendation to a binding Decision 13
3. Problems associated with a binding decision by the EU-Commission according to Art. 19 FDR 14
   - 3.1 Timeframe for a decision 14
   - 3.2 Are the preconditions for a decision given? 14
   - 3.3 Simply Changing the Principle of Cost-Orientation with Comitology? 15
   - 3.4 Weakening National Regulatory Authorities' Independence 15
   - 3.5 Absence of the Right for the Commission to Veto Remedies 16

V. The Netherlands as a Test Case: Current Developments 17

1. The Case 17
2. Interpretation of Facts 17

VI. Scenarios in case of an MTR-decision 18

VII. Conclusion 19

I. Introduction

Mobile Termination Rates (MTR) are the fees charged by one mobile network operator to another network operator for carrying calls coming from another network onto its own mobile network.

In all EU-Countries, MTR are subject to regulation by the respective national regulatory authority. The European Commission has expressed its dissatisfaction with existing differences between these national regulatory approaches. In its legally non-binding MTR-recommendation, in 2009, the Commission has put forward its ideas on how MTR should be regulated.

The reason for us addressing this well-commented Recommendation once again, is the following. With the revision in December 2009 of the Telecommunications-Framework Directive (2002/21/EC), the Commission was given the power to transfer non-binding recommendations into binding decisions after a certain period of time. In the MTR-Case, following our deliberations, the Commission should be able to do so by December 2011.

This paper is organised as follows: In Section II we shortly discuss the Commission's ideas on how to regulate MTR in the future. Section III offers an economic assessment of the Commission's proposals. We very shortly dwell on the necessity to regulate MTR at all, before dealing in more detail with the regulatory concept of pure long-run incremental costs (pure LRIC) advocated by the Commission. In making clear its implications, we will argue that this regulatory approach is unsustainable, assumptive and arbitrary. Finishing this section, we will critically appraise the necessity for regulatory action by the EU and for symmetric termination rates. Section IV shortly deals with the non-binding character of EU-Recommendations before discussing the Commission's power to convert the recommendation into a binding decision and problems associated with this. Section V gives a short list of scenarios in case the Commission adopts an MTR-Decision. Section VII concludes.

II. The EU-Commission's MTR-recommendation 2009/396/EC

1. Content

After consulting industry as well as national authorities, the EU Commission issued a non-binding recommendation on the treatment of Mobile Termination Rates (MTR) in May 2009.[1] The Recommendation is addressed to all Member States and their national regulatory authorities.

With reference to markets for wholesale voice call termination on individual public telephone networks[2], in this "MTR-recommendation" the Commission calls upon national regulatory authorities to "set termination rats based on the costs incurred by an efficient operator".[3] The Commission recommends national regulatory authorities to value these costs on the basis of a bottom-up model using current costs and long-run incremental costs (pure LRIC).[4]

The Commission defines "incremental costs" as "costs that can be avoided if a specific increment is no longer provided".[5] Other than in traditional "Long-Run Average Incremental Costs (LRAIC) models, in the pure LRIC Model, incremental costs are not necessarily driven by a small increase in overall output of an operator. The increment can be defined very narrowly in order to only include costs related to a specific services offered by an operator.[6]

In applying the LRIC-Model in the MTR-case, the Commission recommends national regulatory authorities to define the wholesale voice call termination service provided to third parties as "relevant increment". Hence, incremental costs are to be seen as the difference between "total long-run costs" of an operator providing a full-range of telecommunication services (including wholesale termination) and total long-run costs of an identical operator, which does however not provide these wholesale termination services.

The Commission wants national regulatory authorities not to take account of costs which are "non-traffic related".[7,8] Hence, only the residual of traffic-related costs which can be attributed directly to wholesale termination services (and not to other services) can be taken into account by national regulatory authorities when setting wholesale termination rates. In attributing traffic-related costs, these costs should first be allocated to services other than wholesale termination. Only residual traffic-related costs should be allocated to wholesale termination services.[9]

The Commission makes clear that it interprets "traffic related costs" in a very narrow way. Costs incurred by operators to guarantee coverage and costs caused by the used of spectrum frequency are seen as not traffic driven and are hence not to be taken account of when calculating termination rates. Only additional capacity and spectrum investments, which are necessary to "carry increasing levels of traffic" can be seen as traffic-driven and may be taken account of.[10]

[1] Commission Recommendation 2009/396/EC on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU of 7 May 2009, Published in OJ L 124, 20 May 2009, pp. 67 - 74.
[2] European telecommunication regulation refers to "markets" which are predefined by the EU-Commission in non-binding "Market Recommendations". At the time of issuing its MTR-recommendation, the relevant market recommendation was Recommendation 2003/311/EC of 11 February 2003. On 17 December 2007, the Commission issued a new Market Recommendation (2007/879/EC), which is in place up to this date.
[3] MTR-recommendation, Nr. 1.
[4] Id. Nr. 2.
[5] Id. Nr. 5.
[6] Commission Staff Working Document, SEC(2009) 600, p. 14.
[7] Traffic-related costs are defined by the Commission as all those fixed and variable costs which rise with increased levels of traffic.
[8] Annex to MTR-recommendation, „The non-traffic-related costs should be disregarded for the purpose of calculation wholesale termination rates".
[9] Id.
[10] Id. Annex.

Moreover, the Commission makes clear, that MTR should "normally be symmetric" (meaning: equal for all operators) and that "asymmetry requires an adequate justification".[11] The Commission sees a need for symmetric prices also between established operators and later entrants. It is willing to accept higher MTR for new entrants for a period of four years since entry into the market only.[12]

The Commission calls upon national regulatory authorities to implement the non-binding Recommendation by 31 December 2012.[13] National regulatory authorities can set interim prices on the basis of model other than LRIC until 1 July 2014, given the outcome of this model is "consistent" with those of the LRIC-Model. After that date, only when "objectively disproportionate" a national regulatory authority may continue to apply another model. However, prices resulting from the application of other models "should not exceed the average of termination rates set by national regulatory authorities" implementing the LRIC-Model.[14]

2. Possible next step: A Binding Decision according to Art. 19 FDR

Shortly after the issuing of the MTR-recommendation in May 2009, the updated European Telecommunication Framework Directive (FDR) entered into force.[15] This new directive enables the Commission to issue a legally binding decision if – two years after the issuing of a non-binding recommendation – divergences in the implementation by national regulatory authorities of European rules still cause barriers to the internal market.[16]

[11] Commission Staff Working Document, SEC(2009) 600, p. 9.
[12] See Commission Staff Working Document, SEC(2009) 600, p. 19. The Commission believes that it „can be expected to take three to four years [for a new entrant] to reach a market share of between 15 and 20%".
[13] Id. Nr. 11.
[14] Id. Nr. 12.
[15] Directive 2009/140/EC amending Directive 2002/21/EC.
[16] Art. 19 FDR

III. An Economic Assessment of the MTR-recommendation

1. Need for MTR-Regulation

The question whether or not an ex-ante regulation of MTR is economically necessary is beyond the scope of this paper and will not be dealt with in detail here. Economic literature tends to advocate a regulation, based primarily on the argument that termination on mobile network is an essential input to enable competition. Also, ever single network operator is in essence a non-contestable monopolist, as substitution for termination into a specific mobile network is not possible. This idea of *one network* being *one market* makes a strong case for regulation. Moreover, as Höffler argues convincingly, it is very doubtful whether Ramsey-Boiteux pricing ideas can contribute to the MTR discussion. It is questionable whether pricing in the absence of regulation would be welfare maximising.[17]

Two arguments against regulation MTR deserve special mentioning.

In the EU, MTR are billed to calling parties ("calling party pays", CPP). Changing this as to make the receiving party pay (RPP) for termination of calls may cause customers to take into account these MTR when deciding upon signing a contract with a mobile operator. This may steeply increase competition on the MTR-Market, making regulation unnecessary.[18]

Also, alternative to MTR being billed between different calling parties, an option is to make network operators "bill and keep" there termination rates. This would save transaction costs and seems especially useful if mobile networks are of a similar size, as MTR-payments then come close to a zero sum game.[19,20]

At least for the moment, it seems highly unlikely that these changes of an institutional character have any chance of being put in practice in the EU. Given this imperfectness, we see a need to regulate MTR.

2. Regulating with the Pure LRIC Model

2.1 Pure LRIC: what does it really mean?

The implications of the pure LRIC Model are far reaching. Most likely, the pure LRIC will lead to regulated MTR-prices not covering costs. The reason for that is the combination of

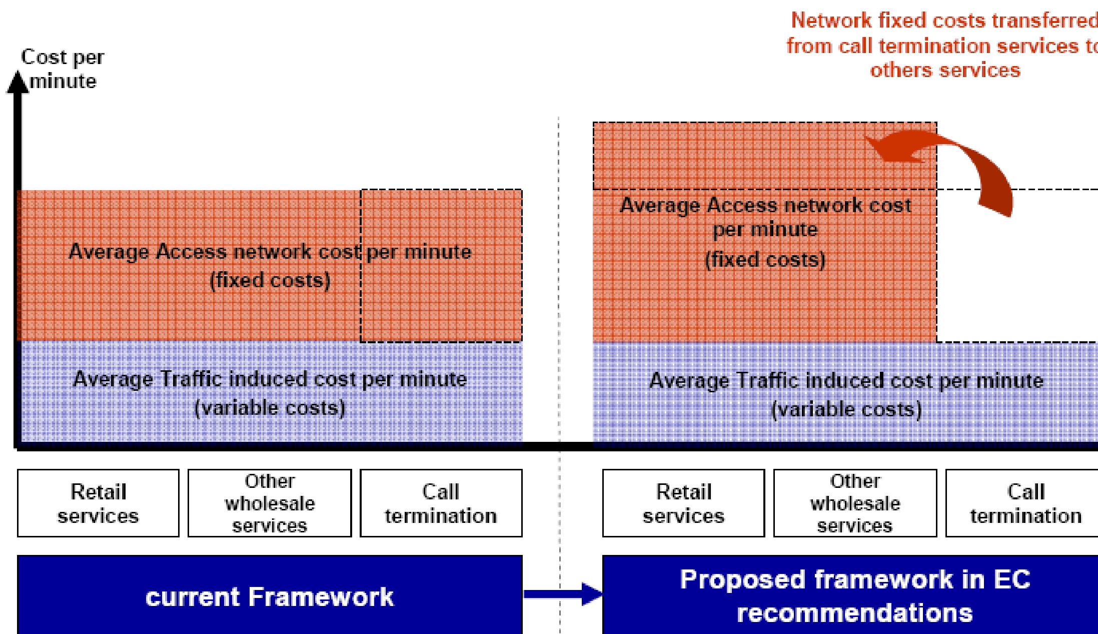
- defining a specific "increment" (here: wholesale MTR) instead of an increment in overall output and
- allowing only a very small range of non-traffic related costs to be taken into account when calculating regulated prices for this specific service.

In network-sectors such as telecommunication or energy, which are characterised by high fixed and common costs each single part of the complete range of services is usually to assist in covering

[17] Höffler (2005), Monopoly Prices versus Ramsey-Boiteux Prices: Are they Similar, and: Does it Matter?, Preprints of the Max Planck Institute for Research in Collective Goods, 2005/7, Bonn.
[18] Amongst others, see Littlechild, S. (2006) "Mobile Termination Charges: Calling Party Pays versus Receiving Party Pays," Telecommunications Policy, 30, 242-277 or Dewenter, R. and Kruse J. (2010), "Calling party pays or receiving party pays? The diffusion of mobile telephony with endogenous regulation", Information Economics and Policy 23, 1, pp. 107-117.
[19] See: Monopolkommission (2009), Sondergutachten Telekommunikation 56: „Klaren Wettbewerbskurs halten" at Nr. 170.
[20] This is true only for the relationship between mobile networks. Fixed and virtual networks are not taken account of in this reasoning.

these common costs. A regulatory approach not allowing for this, risks an undercoverage of fixed and common costs by regulated prices.

In the concrete example of MTR, this means that the bulk of costs which are common to call termination and other services (such as for example call origination) must not be covered by MTR-prices. In different words: costs for planning, building and maintenance of mobile networks must be covered by (higher) prices for other mobile services (see graph below).



Pure LRIC for MTR: a graphical overview[21]

As these costs need to be covered in some way, this regulatory approach inevitably leads to cross-subsidies within the spectrum of mobile services, known as the “waterbed-effect”. Price increases for other mobile telephone services will be necessary to compensate for losses causes by the MTR price change. This may include price changes for phone minutes but also for fixed monthly mobile contract payments.[22]

2.2 Pure LRIC: Three Arguments Against

It is important to point out that the pure LRIC approach intentionally leads to regulated prices, which differ from those which would occur in a competitive environment. Such prices, which the traditional regulatory model (LRAIC) intends to mimic, allow for the recovery of fixed and common costs by all regulated parts of the service spectrum. The pure LRIC explicitly does not allow this to happen for MTR.

This important discrepancy between both models reflects a fundamental difference about the aim to be reached with regulatory policy.

[21] Taken from: Study on the future of interconnection charging methods, Tera Consultants, Study for the EU-Commission, 23 November 2010.
[22] An estimate of changes is given by Frontier Economics, Assessing the Impact of Lowering Mobile Termination Rates, July 2008 and Ofcom, Wholesale Mobile Voice Call Termination, Market Review, Volume 2, April 1st 2010.

The traditional LRAIC Model "simply" aims at setting regulated prices such, as they would occur in a competitive environment. This approach abstains from any further ambitions to fine-tune prices.

The pure LRIC however, is far more ambitious. Its aim is to willingly set regulated prices which deviate from competitive ones. The point of this fine-tuning is similar to internalising external effects, in order to reach an aim akin to an "optimal welfare result".[23]

We believe the latter pure LRIC model should not be pursued. In our opinion it is **unsustainable** and is likely to lead to **arbitrary results**, which are to a high degree subject of political influence-taking. Above all, it **presupposes knowledge to an extent which is simply not present.**

The pure LRIC model is **unsustainable**: were the Commission to apply this model to all subsets of mobile telecommunication services, mobile operators would be forced to charge prices which do not cover fixed and common costs. In network sectors, these costs are very comprehensive and cannot be neglected. Hence, a general application of the pure LRIC model would inevitably make it uneconomic to mobile operators to provide services at all.

The application of the pure LRIC model to MTR forces operators to attempt to cover for fixed and common costs via price increases for other services. If all these services were price-regulated under a pure LRIC approach, this would however not be possible. The pure LRIC model can hence not be example on how to regulate network industries.

This makes clear, that the choice, which part of the telecommunication services spectrum is regulated by a pure LRIC approach is rather **arbitrary**. The Commission could as well decide to regulate wholesale bitstream (just to name one) instead of MTR on a pure LRIC basis. An economically convincing explanation, why exactly MTR should be regulated in this manner, is not clear.

This is even more the case, as the method proposed by the Commission to estimate the actual costs of the relevant increment (Mobile Termination) seems quite absurd. The Commission envisages to estimate these costs by considering two efficient mobile operators: one offering the full scope of mobile telecommunication services; the other offering *all but* termination services. The difference in costs between both should then be seen a "true costs" of termination. In practice however, no mobile operator does *not* offer the termination of calls on his network, as this would mean that external calls cannot be received on his network.

It seems as the decision to regulate MTR on a pure LRIC basis is **driven** more **by the political agenda** of the EU-Commission than by network-economic arguments. The Commission has indeed made clear on numerous occasions that in its opinion, current MTR are too heterogeneous and too high.[24] It may be no coincidence, that such a desire for lower MTR may very well be fulfilled by applying the pure LRIC model to exactly MTR.

On other topics as well, the Commission has shown to have a particular interest in a specific outcome of regulation: lower prices. It would not surprise, if the Commission were to propose the application of the pure LRIC model for those topics in the near future as well. Attention is drawn in this context to the Commission's Roaming initiatives[25], putting in place lower roaming prices directly by means of regulation. Striking as well are the Commission's youngest deliberations on costing methodologies for key wholesale access prices in electronic communications.[26] As

[23] In its impact assessment [SEC(2009) 599], the Commission even attempts to calculate the positive impact on overall welfare of this approach and ends up with a positive estimate of 1 Billion € over a range of six years. (pp. 16 – 30).
[24] See e.g. COM (2010) 253 final/3, "Progress Report on the single European electronic communications market 2009 (15th Report), 25.08.2010 at p. 8 or SEC(2010) 630 final/2, Commission Working Document, 25.08.2010 at pp. 51-52.
[25] Regulation EC 544/2009.
[26] See: http://ec.europa.eu/information_society/policy/ecomm/library/public_consult/cost_accounting/index_en.htm.

consultation papers make clear, the Commission seems to be looking for a way to influence regulated copper access prices such as to boost NGA-Investment.

All this makes clear, that the pure LRIC approach pursued by the EU-Commission is essentially a regulatory fine-tuning approach. The Commission aims at fine-tuning regulated prices, by willingly setting regulated MTR-prices which differ from competitive prices in order to correct for externalities and reach something like a "welfare maximising" level in terms of prices or market organisation.

In our opinion, such an attempt is assumptive and doomed to fail.

Nobody, not a European Commission, national regulatory authorities nor the best expert **can claim to have the knowledge necessary to decide which regulation** or price level will **be "welfare maximising"**. Doing so blatantly ignores the fact that (mobile) telecommunication markets are highly dynamic and that future evolution simply cannot be predicted. It shows a high level of arrogance, since in essence bureaucrats claim to perfectly know the consumer's (future) preferences and hence "just have to turn some screws" to make this consumer "happy".

Disposing of such knowledge is not possible[27]. Hence the Commission as well as regulators should be more modest in their efforts. They should not – by means of a pure LRIC model – attempt to internalise all kinds of network externalities (without specifying which ones) in order to "maximise welfare" (whatever that might be). This will unavoidably patronise customers and lead to a misallocation of capital.

The – ambitious enough, but more modest – LRAIC approach seems more promising, as it abstains from internalising whatever externalities one might claim to perceive. The result will be prices attempting to mimic a competitive situation; leaving any further fine tuning to instruments outside the scope of network regulation (e.g. taxes).

3. Need for Intervention by the EU-Commission

In Part 2 we discussed the problems connected with the pure LRIC model advocated by the EU-Commission. In this Part, we discuss the question whether there is a necessity for intervention by the Commission in MTR-regulation at all.

In our view, there is no clear case for the EU-Commission to intervene in the regulation of MTR. The service of terminating mobile calls is a national market.

The degree and design of national regulation in this market has no impact on other European markets or foreign customers. It is not clear how a national regulatory authority's MTR decision would affect foreign consumers more than domestic ones; nor is preferential treatment by national regulators of national champions (so called "strategic regulatory policy") feasible.[28]

We also do not see how using an identical pure LRIC approach for all MTR in all Member States is necessary to lower transaction costs and hence boost the (competition in the) internal market. We agree that predictability of the (future) MTR regulation may well be very important to mobile operators which consider offering services to customers in different Member States. For this, it does however not need an identical pure LRIC approach in all Member States. National MTR-regulation which is well-documented, cost-based and transparent is predictable as well.

[27] See for example, Friedrich A. Hayek, The Use of Knowledge in Society, American Economic Review XXXV, No. 4. pp. 519-530.

[28] See also: Haucap J , "The Recommended Regulation of Fixed and Mobile Termination Rates: A Critical Appraisal", Monitoring EU Telecoms Policy 2009 at pp. 29 - 30.

Put in economic terms: there are no cross-border externalities which should be internalised by a European – instead of national – regulation. We see no need for the Commission to intervene in MTR-Regulation.

Even more, a European obligation for national regulatory authorities to use the pure LRIC approach when regulating MTR comprises risks as well. Forcing all national regulatory authorities in using the same model makes mutual learning impossible. Possible regulatory errors inherent to the model will be made in all EU-countries. Given the assumptive character (see above) of the pure LRIC approach, this danger seems very real. Acting mistakenly as an "all-knowing" regulator in the same way, in all 27 Member States is likely to lead to high welfare losses.

4. Harmonisation and Symmetry

Regardless of these arguments speaking against EU-intervention in MTR-Regulation, the Commission has made clear that it is not willing to accept the existing levels of MTR across Member States.[29]

Reading between the lines, it seems as if the Commission actually not just wants national regulatory authorities to use the same pure LRIC approach; but also wants them to reach similar conclusions. The Commission makes clear that it expects future MTR-Prices in the EU to move between 1,5 and 3 eurocent.[30]

Such expectations are to be seen very critically. Differences between member states – be it because of cultural or geographical reasons – leading to different costs should be fully taken account of when regulating prices. Reaching similar prices across the EU cannot be an aim by itself. If not justified by costs, such artificially similar MTR-remedies would distort competition.

Concerning MTR-remedies on a national level, the Commission has made clear in its Recommendation that MTR should "normally be symmetric" (meaning: equal for all operators) and that "asymmetry requires an adequate justification".[31]

As Haucap correctly points out, the Commission's opposition against asymmetric national MTR-remedies seem inconsistent.[32] It is not clear why the Commission at the one hand endeavours to fine-tune termination rates, but at the other hand abstains from using asymmetric MTR-remedies as an instrument to influence market entry, which may well affect welfare. If the Commission were really convinced of its fine-tuning approach, why does it forego the change to further fine-tune by allowing for asymmetric MTR?

[29] See footnote 24.
[30] See e.g. Viviane Reding, Speech/09/222 or SEC(2009) 599, Commission Working Document, 07.05.2009 at pp. 19.
[31] Commission Staff Working Document, SEC(2009) 600, p. 9.
[32] See Footnote 28.

IV. A Legal Assessment

1. At Present: Recommendations and "comply or explain"

Recommendations have in principle no binding force (Article 288 (5) TFEU). However, recommendations (such as the MTR-recommendation) pursuant to Article 19 (1) of the Framework Directive[33] call upon Member States to "ensure that national regulatory authorities take the utmost account of those recommendations in carrying out their tasks. Where a national regulatory authority chooses not to follow a recommendation, it shall inform the Commission giving the reasoning for its position."[34]

It is however fair to say, that there is a certain pressure on national regulatory authorities to comply also with European "expectations", which are legally not binding. When national regulatory authorities deviate from such expectations, they regularly have to anticipate high costs in "explaining" their "non-compliance". Hence, also recommendations which are legally not binding, do – in a way comparable with "soft law" – exercise a high amount of pressure on national regulatory authorities.

Hence, the general trend in Telecommunication regulation in the EU is that the large majority of regulatory issues is discussed on a European level, consisting of the 27 national regulatory authorities, the EU-Commission and BEREC. This goes also for issues, for which such European discussion is not obviously prescribed in EU law. In such a context, national deviations from European "expectations" get more and more difficult, even when those expectations do not foot on a legally binding obligation.

Two examples may clarify this.

First: In December 2008, the Commission requested the German telecoms regulator (Bundesnetzagentur) to notify all draft MTR-remedies in the procedure of Article 7 Framework Directive to it.[35] According to the Commission, the setting of the level of MTR-remedies has a clear cross-border effect.[36] At the same time, the Commission announced that it considered opening an infringement proceeding for non-compliance with EU legislation, if the Bundesnetzagentur continued to fail to notify its draft remedies.[37] In March 2009, the Bundesnetzagentur decided on new levels of MTR-remedies without prior notification to the Commission and other national regulators.[38] Consequently, the Commission opened an infringement proceeding against Germany in June 2009.[39] In June 2010, it sent a formal request to Germany to comply with its obligation under EU law, which took the form of a letter of formal notice.[40] This constitutes the first step of the pre-trial proceedings necessary to be able to refer a Member State to the European Court of Justice (Article 258 TFEU).

The Bundesnetzagentur argued that the German telecommunications law (Telekommunikations-gesetz) prescribes the involvement of the Commission and the other national regulators only for market definitions, market analyses and (abstract) regulatory measures. Concrete regulatory remedies in the fee approval procedure are not to be notified. The Commission on the other hand

[33] Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communications networks and services (Framework Directive).
[34] FDR Art. 19 (1) in the version relevant at the time of the Commission issuing the MTR-recommendation.
[35] IP/08/1860.
[36] See above.
[37] See above.
[38] IP/09/1008.
[39] See above.
[40] IP/10/804.

brought forward the argument that these remedies are also part of the market analysis and must therefore be notified.

In order to put an end to the procedure, the Bundesnetzagentur finally agreed to notify draft MTR remedies.

Even though the reaction of the Bundesnetzagentur prevented a clarification by the European Court of Justice, it is beyond dispute that the Commission does not have a veto power concerning these (concrete) remedies. This means that the Bundesnetzagentur can in principle freely decide on MTR-remedies.

Secondly – this "free decision" on remedies is restricted by very strict procedures in the FDR.[41] Even though the EU-Commission cannot veto national regulatory remedies, it may delay the adoption by national regulatory authorities of remedies. In that case, the Commission, BEREC and the national regulatory authority "shall cooperate closely" to find "the most appropriate and effective measure".[42] If BEREC shares the Commission's doubts on the draft remedy, the national regulatory authority shall "cooperate closely" with BEREC. If the national authority sticks to its plans, the Commission may issue a recommendation, "requiring" the authority to amend or withdraw the draft measure. Finally, the national authority must provide a reasoned justification when not obeying the Commission's recommendation.

2. In the Future: Moving from a Recommendation to a binding Decision

Even though the legally non-binding recommendation may already exercise a considerable amount of pressure on national regulatory authorities, the Commission may even go a step further. The revision of the FDR in December 2009 has brought an important change, which has attracted relatively little attention up to today. This may well change rapidly.

According to the new rules, the Commission may, two years after issuing a non-binding recommendation, adopt a binding decision on the "identification of a harmonized or coordinated approach" in order to get away with the "inconsistent implementation of general regulatory approaches by national regulatory authorities on the regulation of electronic communication markets in the application of Articles 15 and 16 of the Framework Directive, where it creates a barrier to the internal market".[43]

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) RRL 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.

[41] See Art. 7a of the FDR.
[42] Id. Art. 7a (2).
[43] Art. 19 (3) FDR.

3. Problems associated with a binding decision by the EU-Commission according to Art. 19 FDR

A binding decision by the EU-Commission would create a number of legal difficulties. In the following, a short overview is given. A detailed discussion on every single topic is outside the scope of this paper.

3.1 Timeframe for a decision

The Commission adopted the MTR-Recommendation in May 2009, thus before the entry into force of the newest Framework Directive. Only this newest version of the Framework Directive however, enables the Commission to issue the binding decision, two years after issuing a recommendation on the topic.

It is not yet clear, whether the recommendation which the Commission might wish to convert into a decision must already have been adopted under the current version of the Framework Directive or not. At the moment of issuing the recommendation (May 2009) national regulatory authorities were not yet in a position to anticipate that, two years later, a binding decision might follow. This anticipation can only been assumed starting – at the earliest – on 19 December 2009, when the newest Framework Directive came into force.

Hence one might well argue that the Commission – starting this date – is to give national regulatory authorities two years time to comply with the recommendation and can only issue a binding decision by December 2011.

3.2 Are the preconditions for a decision given?

Article 19 FDR states the preconditions for the Commission to issue binding decisions. These are in essence threefold:

- there must be "divergences in the implementation" (Art 19 (1)) or an "inconsistent implementation" (Art. 19 (3)) by national regulatory authority, which
- concern the "general regulatory approach" of Art 15 and Art. 16 FDR (Art, 19(3)) and which
- "create a barrier to the internal market" (Art. 19 (3)).

It is by no means clear that these conditions are fulfilled and the Commission may issue an MTR-Decision prescribing national regulatory authorities to apply the pure LRIC approach.

On the first and second criteria: 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 such as the pure LRIC approach are the methodological basis for decisions made by national regulatory authorities regarding the exact design of regulatory remedies. However, these remedies may 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 are not necessarily part of the market definition and market analysis process. Accordingly they would fall outside the scope of Art. 15 and 16 FDR and hence cannot be the subject of a binding decision.

Moreover, it is very debatable, whether the refusal of a national regulatory authority to use the pure LRIC approach can really be seen as an "inconsistent implementation" of the "general

approach". Unequal decisions are not necessarily inconsistent. Also, differences between national regulatory authorities on this very final step of the regulatory process (i.e.: the costing methods used leading to remedies) are not necessarily so important as to be described pompously as inconsistent regarding the general regulatory approach.

On the third criteria: we have argued above that MTR-Markets are national markets and MTR-Regulation by national regulatory authorities does not seem to show any external effects in other countries. We hence do not see how different costing-methods may cause a barrier to the internal market.

3.3 Simply Changing the Principle of Cost-Orientation with Comitology?

It should well be noted that the Commission cannot issue a decision by itself; European Parliament and Council are involved (regulatory procedure with scrutiny, below simplifying: "comitology"). Comitology – replaced by the Treaty of Lisbon by the system of delegated acts and implementing acts[44] – can be seen as a hybrid form, somewhere in between legislative and executive action.[45] Even though European Parliament und Council are involvement, they do not have the same powers as under the ordinary legislative procedure.

We identify the following difficulty with an MTR-decision adopted in comitology procedures on the obligatory use of the pure LRIC approach.

Any decision taken in comitology may amend only "non-essential elements of the (framework) directive".[46] "Essential" changes are to be made by using the ordinary legislative procedure. Given the fact that it is an established principle that regulated prices should be cost-oriented[47], we find it rather surprising that such an established principle should be changed by means of simple comitology.

Put in a different way: in our opinion, forcing national regulatory authorities by means of decision to use the pure LRIC approach is a change which is "too essential" to be made in comitology procedures.

3.4 Weakening National Regulatory Authorities' Independence

Obliging national regulatory authorities to use the pure LRIC approach is weakening their independence. This independency – which by no means is absolute – is regulated in the FDR, which states: "national regulatory authorities "shall act independently and shall not seek or take instructions from any other body in relation to the exercise of these tasks".[48]

Interestingly, in the (very similar) field of regulation by national regulatory authorities of markets of electricity and gas, this independency requirements have been written down even clearer: national regulatory authorities "do not seek or take direct instructions from any government or other public or private entity when carrying out their regulatory tasks."[49]

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[44] Art. 290, 291 TFEU.
[45] For a detailed study on comitology, see: CEP, "Komitologie, Stand und Aussichten", available at: http://www.cep.eu/en/analyses-of-eu-policy/institutional-law/comitology/.
[46] Art. 19 (4) FDR.
[47] See Art. 13 Access Directive (2002/19/EC) as well as European Court of Justice C-55/06, Arcor/Commission.
[48] FDR Art. 3 (3).
[49] Art. 35 (4), b of Directive 2009/72/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in electricity and repealing Directive 2003/54/EC and Art. 39 (4), b of Directive

We believe it deserves a serious debate, whether an MTR-decision would be compatible with the wish – also by the Commission – for independent national regulatory authorities. In our opinion it were better, when such an important decision as the prescription of a pure LRIC model were done in the ordinary legislative procedure.

An MTR-decision, adopted in comitology procedures, inevitably has characters of executive – instead of legislative – action. Influencing national regulatory authorities by executive actions should be avoided, as it opens the door for a political exerting of influence which is insufficiently backed on a democratic level. In this context, we feel it is useful to point to the fact that national regulatory authorities should shown a great deal of independence not only vis-à-vis Member States, but also vis-à-vis the EU-Commission. It were too simply and naive to see the Commission as non-political, technocrat institution without political ambitions.

3.5 Absence of the Right for the Commission to Veto Remedies

When updating the Framework Directive, the Commission was not able to convince the necessary qualified majority in the Council to assign it with a veto against draft regulatory remedies by national regulatory authorities. [50, 51] The Commission was hence not granted this veto-power, but can apply the procedure described above in accordance with Art. 7a Framework Directive.

An MTR-decision on the obligatory use of a pure LRIC approach would make this denial of a veto right on remedies meaningless. In our opinion, such a decision would blatantly ignore the intention of the European legislator.

The reason why such decision makes the absence of a veto meaningless is the following: prescribing a pure LRIC approach influences quite directly not just one, but even a number of remedy decisions by national regulatory authorities. As it is more abstract than a single veto, but has a huge impact on the design of remedies, such decision is to be seen as more powerful than a veto right.

Upon adopting the Framework Directive in the Council, sixteen Member States (Austria, Bulgaria, Estonia, Finland, Germany, Ireland, Italy, Latvia, Malta, Poland, Portugal, Rumania, Slovakia, Slovenia, Spain and UK) adopted a declaration stating that:

"These Member States therefore considers that the scope of the Commission's decision-making powers under Article 19 of the Framework Directive by reference to Articles 15 and 16 of the Framework Directive is limited to matters concerning market definition, assessment of significant market power and the effect of market analysis on whether obligations should be imposed or not on undertakings <u>but does not extend to the choice and design of remedies under Articles 8 of the Access Directive or Article 17 of the Universal Service Directive."</u>[52]

With this declaration, a high number of Member States made clear, that the Commission should not attempt to use its power under Article 19 to bypass the lack of a veto right against remedies. Applied to our case: these Member States should deny the power for the Commission to adopt a MTR-Decision.

2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC.

[50] The Commission does has the right to veto market definitions and market analyses. (Art. 7 FDR)

[51] For an overview of the legislative process on the new FDR, see http://www.cep.eu/en/analyses-of-eu-policy/telecommunications/electronic-communication/.

[52] See Council of the European Union, Document 15864/09 ADD1 REV1, 18 November 2009, p. 4.

V. The Netherlands as a Test Case: Current Developments

The whole complexity of Article 19 Decisions in MTR-Questions can be well demonstrated using the ongoing case of the Dutch Telecommunications Regulatory Authority (OPTA).

1. The Case

On July 7th 2010, OPTA imposed MTR-Remedies, which were based on the pure LRIC approach. However, on August 31th 2011, the Dutch Trade and Industry Appeal Tribunal turn down this approach in final appeal and ordered OPTA to use a pure LRIC *plus* methodology.

Accordingly, OPTA departed from the pure LRIC approach. It modified its MTR-Remedies upwards and notified these to the EU-Commission on January 12th 2012.

On February 13th 2012, the Commission decided to temporarily suspend these new MTR-Remedies by OPTA. [53]

The Commission has the power to do so according to (new) Art. 7a FDR. Although explicitly not having to power to veto remedies, the Commission may delay the implementation of remedies proposed by a national regulatory authority for three months.

In the concrete case, the Commission argues that OPTA's MTR-Remedies are non compatible with Community Law and create a barrier to the internal market.[54]

In the next six weeks, BEREC will issue an opinion on the matter; deciding whether it shares the opinion on the EU-Commission. This opinion is adopted with a simple majority. There is no obligation for OPTA to follow this opinion.

In a number of cases, the Commission will be able to – in the fourth month after its suspending OPTA's MTR-Remedies – issue a non-binding recommendation to the national regulatory authority in question. Within one month of this recommendation, the national regulatory authority may adopt a final remedy.

2. Interpretation of Facts

Art. 7a FDR does in no way offer the Commission the possibility to veto OPTA's MTR-Remedies. However, the fact that the Commission decided to initiate the Art. 7a proceedings against OPTA signals that the Commission is not willing to accept the opinion of the Dutch Trade and Industry Appeal Tribunal and is exercising pressure on OPTA to come in line with the Commission's interpretation instead of with the one by the Tribunal.

Making BEREC issue an opinion on the pure LRIC issue can be seen as the Commission testing political support for the pure LRIC method amongst member states. If such support were present to a sufficient extent, the Commission may well feel invited to attempt to issue a binding decision according to Art. 19 FDR.

[53] See SG-Greffe (2012) D/2859

[54] See SG-Greffe (2012) D/2859 at p. 5. The Commission sees incompatibilities with Art. 8(4) Access Directive and Art. 16(4) FDR.

VI. Scenarios in case of an MTR-decision

In case the Commission does aim at issuing a MTR-decision and is capable of passing it under the comitology procedure, we see the following scenarios:

1. Certain Member States bring the Commission before the European Court of Justice, claiming that the decision goes beyond competences given to the Commission by the FDR.

2. All national regulatory authorities comply with the decision when setting MTR-remedies.

   In that case a mobile operator may proceed in national court against remedies of the national regulatory authority based on the pure LRIC approach. The Court may reject the claim. It cannot however not be excluded that the national courts refers the case to the ECJ to clear remaining questions. The national courts may also directly annul the national regulatory authority's decision. In that case, a serious conflict would arise and the regulatory situation would be very different amongst Member States.

3. One or more national regulatory authorities do not comply with the decision when setting MTR-remedies.

   In that case, accepting the non-application by the national regulators of the pure LRIC approach would mean nothing else than accepting a breach of European law, leading to serious differences in competitive conditions within the European single market. How exactly the Commission as guardian of the Treaties would convincingly justify this situation seems unimaginable.

   Hence

   a.) the Commission may refer the case to the EU Court of Justice pursuant to Article 258 TFEU (infringement proceedings). This legal remedy requires preliminary proceedings including two procedural steps. In a first step, the Commission sends a letter of formal notice to the Member State concerned to give him the opportunity to submit its observations. Then, the Commission delivers a reasoned opinion. When the national regulatory authority does not alter its behavior, the ECJ may judge whether that behavior is in breach with EU law. In the end of the day, the ECJ will decide whether the MTR-Decision is legally sound.

   Proceeding against a breach before the European Court of Justice is an alternative; which however poses some risks to the Commission. In cannot be excluded, that the ECJ would essentially follow the logic of the Dutch Courts. That would seriously question the legality of the pure LRIC approach within the whole European Union and might lead to a number of other national legislators to refuse to further apply the pure LRIC approach.

   b.) a mobile operator may proceed in national court against remedies of the national regulatory authority as they are not based on the pure LRIC approach. The options here are principally identical to those under Option 2.

VII. Conclusion

Applied to Mobile Termination Rates (MTR), the pure LRIC approach leads to an undercoverage by regulated prices of fixed and common costs incurred by mobile operators. This would have to be compensated by price increases for other mobile services.

We argue that the pure LRIC model should not be pursued. In our opinion it is unsustainable and is likely to lead to arbitrary results, which are to a high degree subject of political influence-taking. Above all, it is assumptive since it presupposes an amount of knowledge which is simply not present. The Commission aims at fine-tuning regulated prices, by willingly setting regulated MTR-prices which differ from competitive prices in order to correct for externalities and reach something like a "welfare maximising" level in terms of prices or market organisation. We believe this is over-ambitious. Regulation based on the traditional LRAIC is more modest and will probably be more correct.

In our view, there is no clear case for the EU-Commission to intervene in the regulation of MTR. The service of terminating mobile calls is a national market without cross-border externalities which should be internalised by a European – instead of national – regulation. We see no need for the Commission to intervene in MTR-Regulation.

From the legal point of view, we see a number of severe problems associated with a binding MTR-Decision by the Commission. We believe the preconditions for an MTR-Decision are not given and see a serious conflict with the non-existing political will to grant the Commission a veto-power against remedies by national regulatory authorities. An MTR-Decision would harm national regulatory authority's independence. Dependent on the willingness of national regulatory authorities to accept the Commission's decision, the result of pure LRIC may be more – and not less – variety in MTR amongst MTR.

The Dutch OPTA case concentrates all these economic, legal and political arguments. It is up to the Commission to decide whether it wants to issue a binding decision (causing political stir given the lack of political will by Member States for the Commission to use Art. 19 FDR as it aims to), based of weak economic arguments. As it seems rather unlikely for the Dutch regulator to comply with the decision, the Commission may either accept severe and distorting regulatory differences in the internal market; or run the real risk of the ECJ turning down the pure LRIC approach altogether.

We hence advise the Commission not to adopt an MTR-Decision and to return to the LRAIC approach in regulating MTR. However, the fact that the Commission has just recently initiated an Art. 7a proceeding against OPTA seems to point in another direction.