

## Case Comment

# European Commission signals strong policy shift under the European Electronic Communications Code (EECC)

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On 4 December 2018, the Transport, Telecommunications & Energy Council approved a new legislative framework for the telecommunications sector in the EU, referred to as the European Electronic Communications Code ('the EECC' or 'the Code').<sup>1</sup> The EECC, which is due to come into full effect across the EU Member States by late December 2020,<sup>2</sup> codifies in one single document all the disparate elements of law which make up the EU Regulatory Framework for electronic communications.

### The new policy balance

The Code re-aligns the electronic communications regulatory framework in a manner which strikes what appears to be a different policy balance between the importance of maintaining competition, on the one hand, and the need for the massive investments that are deemed to be necessary to drive the Digital Single Market (DSM) strategy, on the other. As of 2002, the conventional wisdom in the EU had been that consumer welfare can be best achieved through the forces of inter-platform competition, rather than through the removal of obstacles to investment.

The European Commission had originally put forward its proposal for regulatory reform of the telecommunications sector in September 2016, accompanied by a Communication from the Commission setting out how it viewed the future evolution of the sector. This was seen in the broader context of the health of the European economy, whose dependence on the deployment of future networks was set out in rather stark terms in the Commission's Gigabit Society Communication.<sup>3</sup> The achievement of this vision of a future European economy highlights the need for heavy upgrades to existing networks for both the fixed and mobile operators across Europe.

Accordingly, one of the principal objectives of the EECC is to foster investments in these new Very High

Capacity Networks (VHCNs).<sup>4</sup> VHCN is essentially about investments in fibre and nothing else. In the case of fixed networks, it is defined as 'Fibre to the Home' or 'Fibre to the Building' (or its 'equivalent' but, as defined, it is difficult to see how it can have a practical equivalent). In the case of mobile networks, it means 'Fibre to the Base Station'.

### Elements of the balancing exercise

Over the course of the legislative negotiations for the EECC, certain aspects of the draft proposal have been diluted. For example, the proposed legislation forgoes a strict sequencing of remedies, which would have seen a much greater emphasis on 'passive access remedies'; only when these had failed would other more intrusive remedies have become available. The final EECC text has removed this strict remedy hierarchy from the final adopted legislative text. Other measures, however, have, if anything, been reinforced through the legislative negotiation process. Ultimately, the Commission's vision of investments being driven by infrastructure-based competition (rather than being based on service-based competition) has survived at least in name.

The Code's new policy balance is pursued in a number of ways. At one level, the Code seeks to enable competitive investments by lowering the costs of deployment for those networks through the enhanced sharing of civil infrastructures (Articles 61, 72 and 73). The Code also seeks to create incentives to investment by ensuring lighter access conditions and higher returns, wherever possible.

To some extent, the Code also seeks to create more transparency and legal certainty for investors by setting out the rules in greater detail, in advance of any statutory interpretation effected by National Regulatory Authorities ('NRAs'). This has arguably created unforeseen difficulties in certain instances, especially because it can be almost impossible to legislate for every contingency (for example,

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1 Including a new Regulation establishing the Body of European Regulators of Electronic Communications (BEREC).

2 In other words, two years after official publication of the EECC, expected to occur on 17 December 2018. The United Kingdom has already indicated its willingness to accept the substantive provisions of the EECC into national Law if this timetable is followed.

3 COM(2016) 587 final 'Connectivity for a Competitive Digital Single Market Towards a European Gigabit Society' SWD(2016) 300 final.

4 VHCNs are defined in Article 2 of the Code as: 'either an electronic communications network which consists wholly of optical fibre elements at least up to the distribution point at the serving location, or an electronic communications network which is capable of delivering, under usual peak-time conditions, similar network performance in terms of available downlink and uplink bandwidth, resilience, error-related parameters, and latency and its variation; network performance can be considered similar regardless of whether the end-user experience varies due to the inherently different characteristics of the medium by which the network ultimately connects with the network termination point'.

the Code's prescriptive rules affecting co-investment models, set out in Article 76 and Annex 4, are extensive and very complex, and may even add to existing levels of uncertainty), with preference usually being given to an approach which confers upon NRAs sufficient flexibility in applying a well understood set of policy principles.

Despite these uncertainties, the cornerstone of all the measures that are aimed at fostering ultra-fast connectivity is a set of regulatory incentives aimed at guaranteeing an adequate return on investment for network roll-out plans, and these only apply when such plans focus on VHCN deployment.

At a very fundamental level, NRAs have a series of primary objectives under the EECC, such as ensuring that a sufficient level of competition exists while consumers are also protected in parallel, with these primary objectives being set out in Article 3 of the EECC. By making the promotion of investment in VHCN a primary objective of EU legislators, NRAs are bound to focus all of their decision-making through this prism to determine what the impact of any of these decisions will be on the deployment of VHCN.

The importance of this specific change in focus (together with the definition of VHCN) on future regulatory policy cannot be overstated. For example, in a mobile context it may be the case that VHCN can be promoted when the price of microwave links (an alternative) is reviewed, with a legitimate question also arising as to how charges related to fibre links might be permitted in regulated Mobile Call Termination Rate calculations. If in practice NRAs really seek to achieve their new policy objective, as opposed to exercising their discretion to pay lip service to it, one cannot exclude that material regulatory changes might ensue, especially given the fact that wireless links are far more prevalent than is realised (as compared to fixed lines to mobile base stations).

## Separation remedies and 'wholesale-only' operators

In terms of specific regulatory obligations laid down in the Code to drive VHCN investments, the momentum to achieve the benefits of this infrastructure-based approach to competition is now laid squarely at the feet of separation remedies. These range from the very specific Article 80 dealing with 'wholesale-only' operators (which have no retail operations and hence, in theory, have no incentive to discriminate against retail competitors), to co-investments made in VHCN where a separate governance structure is likely to emerge in which integrated operators form part of the group of co-investors in network infrastructure. These remedies are prescribed in addition to existing provisions concerning voluntary vertical separation (Article 78) and functional separation (Article 77).

In practice, a wholesale-only operator can be expected to be essentially exempted from most provisions of the Code, even where that operator is designated to hold Significant Market Power (SMP). Somewhat paradoxically, a vertically integrated operator that vertically separates its operations has no guarantee that it will be eligible to be treated as a 'wholesale-only' operator under the terms of Article 80.

While the new Code seeks to render the access rules more focused and legally certain, it limits the situations according to which market access obligations can be imposed in relation to VHCN (Article 68). It also provides NRAs with the possibility (Article 67) of conducting market analyses every five years (as opposed to the current timeframe of every three years). In order to support infrastructure-based competition, the NRAs may oblige operators to satisfy reasonable requests for access to their civil infrastructure, including antennas, towers and poles.<sup>5</sup> However, access to non-replicable network assets is limited in order to safeguard investment incentives, and can be extended only in limited circumstances (for example, to enable alternative network deployment in sparsely populated areas). SMP-designated operators which make investments in VHCNs may also benefit from a lighter form of price regulation (Article 76 and Annex 4). By contrast, wholesale-only operators will again be exempted from strict price controls, even if they are SMP-designated operators.

## 'Known unknowns'

While the evidence to date suggests that wholesale-only operators and their investments are accelerating rapidly, the evidence of integrated operators making a competitive response to such investments<sup>6</sup> is more elusive. The competition implications of such an approach (and, indeed, the long-term investment benefits) are also less than obvious. A wholesale-only business model, in particular, while possibly removing the incentives for the operator to discriminate, also signals very strongly the limits to infrastructure competition, as do all separation remedies. In parallel, the impact of the separation of networks raises very legitimate concerns about investment co-ordination and so-called investment 'hold-up' problems<sup>7</sup> in the future. These risks have been acknowledged by the Commission, but the imperative of achieving VHCN in the short term seems to have been overridden by longer-term investment considerations. As noted in the Commission's Impact Assessment which accompanied the proposals:<sup>8</sup>

5 Article 61 is the most extensive set of general obligations in the Code, and extends the possibility of imposing a general obligation on all operators who control non-replicable wires and cables connecting end-users to the network to give access to the entire loop to competitors where replication of such network elements is economically inefficient or physically impracticable. 'Wholesale-only' operators are more or less exempt from these provisions.

6 For instance, Telecom Italia ([https://seekingalpha.com/news/3410900-telecom-italia-plus-3\\_8-percent-ceo-choice-suggests-new-direction](https://seekingalpha.com/news/3410900-telecom-italia-plus-3_8-percent-ceo-choice-suggests-new-direction)) in Italy and SFR in France (<https://www.totaltele.com/501709/Altice-nets-18bn-from-partial-sale-of-its-French-fibre-unit>) are both looking at different forms of separation to deal with the new competitive threats posed by 'wholesale-only' operators.

7 F. Lafontaine and M. Slade, 'Vertical integration and firm boundaries: the evidence', *Journal of Economic Literature* 45.3 (2007) at 629685.

8 Commission staff working document impact assessment accompanying the document Proposals for a Directive of the European Parliament and of the Council establishing the European Electronic Communications Code (Recast) and a Regulation of the European Parliament and of the Council establishing the Body of European Regulators for Electronic Communications, COM(2016) 590 (COM(2016) 591), SWD(2016) 303 final PART 1/3 (footnotes removed).

As regards *indirect effects*, there is a risk that provisions concerning wholesale-only models may foster separation and therefore increase reliance on regulated wholesale access to the detriment of potential developments in infrastructure-based competition thereby impeding incentives in fast infrastructure investment. On the other hand, it would reassure investors regarding the regulatory approach to local fibre networks whose market power at the local level may be found to be significant. If a single wholesale-only fibre network is deployed, infrastructure competition is also likely to be of lesser relevance in attaining the various objectives of the Framework. Separation or wholesale-only models may result in increased service competition, which may boost broadband take-up through reduced retail prices and service innovation. Moreover the risk of impacting infrastructure competition could be mitigated if separation is incentivised in areas or circumstances where infrastructure-based competition is unlikely to arise.

### The residual role of BEREC

The counterweight to the apparent dilution of regulatory intervention in the sector is arguably found in the wide-ranging role under the Code to be played by BEREC, the European Union's consulting group for NRAs. A surprisingly large role is to be played by BEREC in the articulation of policy in the electronic communications sector, and all of it will occur in the future as the Code is implemented into national laws by December 2020.<sup>9</sup>

It is not unreasonable to assume that many existing regulatory principles may therefore continue to find their way into the post-2020 regulatory regime, especially given the possible consultation role that BEREC might play in the elaboration of rules regarding platform providers (particularly as regards the elaboration of non-discrimination and transparency principles).

### Conclusions

Until now, sector-specific regulators have assumed that existing 'incumbent' owners of infrastructure would have no option other than to invest in infrastructure in order to compete with other network providers (in a sort of 'prisoner's dilemma' scenario, because neither the incumbent nor the new entrant know in advance the level of investment to be expended by the other). Thus, consumer welfare in terms of better network performance was, alongside greater retail price competitiveness, considered to be an integral part of the competitive process. This view was reinforced by the approach of the European Commission in its review of mergers, where the traditional antitrust economics suggested that '4-to-3' mergers were inherently prone to drive up prices in the post-merger environment.

The policy drift of the EECC suggests that the presumption that competition alone will deliver the investments necessary for Europe to achieve its broadband aspirations has been rebutted in practice. Regulatory policy will henceforth give primacy to achieving the longer-term goal of achieving VHCN deployment above the short-term goal of greater broadband retail price competition. Indeed, the grant of unconditional clearance to a 4-to-3 mobile merger in the Netherlands<sup>10</sup> in parallel with the adoption of the EECC suggests – even if only indirectly – that even EU competition law might in parallel be recalibrating its notion of consumer welfare to attribute greater weight to the importance of network upgrades. A strong test of how much EU competition rules are able to accommodate this regulatory policy shift will no doubt be experienced when the Commission has the opportunity to review its current Broadband State Aid Guidelines.<sup>11</sup>

If this is correct, the EU could be witnessing a massive shift in regulatory policy emphasis. Whether or not, however, that official policy line at Commission level materialises in practice across the Member States will depend in large measure on the attitude of NRAs, cooperating with BEREC, in the implementation of regulatory policy in concrete individual situations of enforcement. One should not be surprised if, at the ground level of policy enforcement, change in policy is not as far-reaching as many policymakers in Brussels might be anticipating.

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<sup>9</sup> An idea of the importance of BEREC's future role in policymaking can be seen in the release on 12 December 2018 of its ambitious Work Programme for 2019, and in the release of a number of public consultation documents covering topics as varied as mobile infrastructure sharing, the termination of customer contracts when switching providers, conditions of access to physical infrastructure, consumer information, regulatory accounting practices and geographic markets analysis. See [http://berec.europa.eu/eng/about\\_berec/annual\\_work\\_programme/](http://berec.europa.eu/eng/about_berec/annual_work_programme/).

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<sup>10</sup> See M.8792, *T-Mobile NL /Tele2 NL*, Commission Decision adopted on 27 November 2018 (unreported).

<sup>11</sup> EU Guidelines for the application of State Aid rules in relation to the rapid deployment of broadband networks, OJ C25/1 of 26 January 2013.