EUROPE IN THE ROUND (PART II)

PETER ALEXIADIS concludes his tour of the trade-offs inherent in communications regulation

This is the second part of an article that explores the fundamental policy drivers that should shape the economic regulation of the electronic communications sector by 2020, with reference to Europe. My approach is not to consider the merits of each individual policy item in its own right, but to explore a range of issues which involve a series of policy trade-offs that legislators and enforcement agencies cannot afford to ignore.

In part one I looked at the first four of seven such trade-offs, namely:

- The twin goals of greater investment and less regulation
- Conflicts between greater consolidation and less regulation
- How pan-European markets respond more to commercial incentives than harmonisation
- Realising the limits to the 'technology neutral' concept.

See Intermedia September 2015 for the article that covers these four trade-offs. I now cover the remaining three.

ACKNOWLEDGING THAT A NEW ACCESS REGIME MIGHT BE NECESSARY

Since the adoption of the 2002 EU regulatory framework for electronic communications, the analytical model used to determine which parties should be subject to wholesale access obligations

has been subject to pressure in five significant respects:

- In the fixed sector, significant losses in market share at the retail level have occurred in the provision of broadband services, while partial substitution has been evidenced for voice services by new applications such as WhatsApp, and the creation of potentially complex oligopoly situations has been identified by some regulators in those jurisdictions where cable TV networks exist.[1]
- The ever-increasing consolidation that has been occurring among mobile operators, and the attendant remedies to which those operators are subject under the EU merger review process.[2]
- A proliferation of symmetric regulation alternatives has occurred through the various revisions to the regulatory framework (including through the recently adopted directive 2014/61/EU).[3]
- The success of local loop unbundling across the EU has been very mixed, and the ability of operators to climb the so-called 'ladder of investment' has been called into question in many member states.[4]
- The patterns of fixed network deployment one finds across the EU are many and varied, especially depending on the particular iteration of next-generation access policy that has been followed by various member states.

What these changes have meant over the course of more than 12 years is that fundamental questions need to be asked as to what policymakers seek to achieve through the access regime – namely, greater competition in retail markets or other industrial policy goals. This will mean that questions are inevitably asked as to whether the current regime which foresees the regulation of operators with significant market power (SMP) continues to remain fit for purpose in light of all the changes that have occurred. Aside from those who might advocate a continuance with the current SMP access regime, there will be those who advocate that mandated access to networks is no longer necessary because of the current state of competition, while others will argue that different regulation is necessary to ensure that competitive access alternatives continue to exist in an environment characterised by increasing consolidation and market exit.

“There are real benefits in allowing the market to deliver competitive network offerings.”

In my view, if trade-offs need to be made, there are real benefits in allowing the market to deliver competitive network offerings in the absence of regulation, at least where withdrawal is based on reasonable assumptions about market entry and where regulatory intervention can be triggered should access alternatives not materialise.

Of the alternative regulatory models available to challenge the SMP regime, some of the models worthy of consideration should be:

- The 'essential facilities' test[5]
- A prescribed 'bottleneck' test[6] which is defined specifically with telecoms networks in mind
- A modified, or sector-specific version of the 'substantial lessening of competition' test[7] currently found in the EU merger regime.

We should discount the possible application of the old open network provision (ONP) model of the 1990s which imposed access obligations on operators with 25% share of a relevant access market,[8] given that its only redeeming feature is its simplicity (and hence, ease of application). However, its character as a 'blunt instrument' does not lend itself easily to the complex policy trade-offs that need to be made.

Of the options set out above, the essential facilities doctrine seems to be setting too high a bar for intervention by regulators, given that it is already a well understood and defined concept under competition rules and is clearly a very difficult standard to satisfy in legal terms. By

contrast, the concept of a bottleneck is already found in the current practice of the European Commission under its administrative practice under the EU regulatory framework. In addition, its sui generis nature provides sufficient flexibility to national regulators to allow a sector-specific definition to be generated which is compatible with the use of 'soft law' instruments that clarify its scope (especially as new technology is introduced).

The sector-specific use of a modified form of the EU merger regime test to identify a 'substantial lessening of competition' (SLC) is not without merit, especially since so much de facto access regulation is being effected through the merger review process (at least in so-called 'gap' cases falling short of collective dominance). Perhaps a sector-specific adaptation of that test might be something along the lines of an 'unavoidable trading partner' test on which to base some form of access regulation where it is felt that an access option is important to sustain competition, irrespective of whether dominance exists at the retail level. However, the introduction of such a flexible test under the EU regulatory framework would in all likelihood also require a change in the current institutional decision-making process shared between national regulators and the European Commission.

In my view, the proposed scheduling of 5G across the EU member states for 2020 will generate such a fundamentally new dynamic in the marketplace (building on the 4G/LTE currently being deployed), that it will be appropriate to modify the existing SMP regime given that traditional concepts of market power might no longer be associated with incumbent fixed line networks and because the concept of 'collective SMP' has proven to be exceedingly difficult to implement in practice.

Moreover, given the increased deployment of fibre to the home in urban areas, one needs to make a realistic appraisal of whether it is retail competition or wholesale access options that need to be promoted; if the former, we should not be surprised if more widespread deregulation in urban areas is the preferred option.[9] By the same token, a departure from the technology neutrality principle could see the possible mandated deployment of open architecture fibre networks (and accessible internal wiring) as asymmetric measures.[10] The possibility also exists that the functional separation regulatory model pioneered in the UK might also provide a basis for the winding-down of other forms of ex-ante regulation.[11]

THE NEED TO IDENTIFY EMERGING MARKET FAILURES

With the fundamental shift in values in the electronic communications value chain, whether it be in the form of partial substitutes from various applications such as WhatsApp,[12] the commoditisation of voice services, the possible proliferation of mobile virtual network operators (MVNOs) from companies such as Google, and the increasing demand for bandwidth-rich and data-rich services, the regulatory impetus might be shifting from the identification of traditional market failures based on network dominance to market failures based on the possession and manipulation of large amounts of data and access to 'eyeballs'. This will be an environment in which over the top (OTT) operators play an increasingly important role, both in terms of providing countervailing bargaining power against traditional operators, by providing indirect pricing constraints against them, and by virtue of being the focal point of new revenue-generating services. As such, their competitive impact will increasingly play a pivotal role in the decisions of national regulators as to whether asymmetric access regulation should be removed or maintained (much as voice over IP communications played a key role in the gradual expansion of voice markets).

“There will be concerns in some quarters that ‘big data’ will be a basis on which to entrench market power.”

However, it will also be an environment where parties with privileged and widespread access to data might be tempted to leverage such access into a wide range of emerging markets, both at the expense of traditional operators and pre-emptively against new entrants (Google's Project Fi, an MVNO that's running across several networks in the US, is a good example). Aside from the potential which exists for certain OTT providers to dominate key bottleneck functions in the developing internet ecosystem, other OTT providers might be capable of adopting commercial strategies designed to produce a lack of service interoperability, especially as user communities globally might dwarf member state populations and lend themselves to being insulated from certain types of competition as vertical technology 'silos' or 'walled gardens'.

Moreover, there will be concerns in some quarters that certain players will be able to harness 'big data' as a means of not only developing attractive service offerings, but also as a basis on which to entrench market power, thereby creating a virtuous circle of increasing market intelligence leading to greater market power, linked by the effects of data manipulation;[13] to this end, insufficiently nuanced data protection and consumer protection rules might unwittingly support such market power insofar as consumers might become increasingly contestable to those operators without access to such data.

These two conflicting roles of OTT providers will inevitably call into question one of the cornerstones of the current EU regulatory framework, namely, whether any of the functions or services provided by such new market actors constitute a legitimate extension of the concept of an 'electronic communications network' or an 'electronic communications service'.[14] To the extent that the EU regulatory framework is expanded to cover such functions or services, however, the ability of the framework to address market failures will need to adapt to be able to take into account a broader range of discriminatory practices and refusals to provide interoperability. This might in turn require a closer form of collaboration between ex-post investigations and ex-ante remedies, which will

exert pressure on changes being made to existing institutional arrangements.

To be able to respond to such rapid commercial developments brought about by the inclusion of a range of new market actors and through the realisation of formidable commercial and technological developments, the regulatory framework will no doubt require a flexible mechanism through which policy directions can be reconsidered for important strategic issues such as bundling, the role of discriminatory practices, margin squeezing across 'converged' service offerings, access to certain types of content, the legitimate scope of the concept of 'specialised services' (in the context of the net neutrality rules which came into force on 30 April 2016),[15] etc.

The resolution of such issues will require flexibility to be able to adapt to new technological and commercial changes, and is likely to herald the introduction of a competition-style approach into a regulatory setting, with the opposite trend already being the case.[16] Given that the net neutrality issue turns on the interpretation of key competition issues such as 'discrimination', the objective justification behind traffic management techniques and the common welfare implications behind the introduction of 'specialised services', the flexibility afforded by a competition-style analysis seems better suited to the resolution of those issues than the prescriptive ex-ante approach.[17] More broadly, it might therefore be helpful to consider whether a greater institutional role should be played by 'sector inquiries'[18] in the assessment of the potential market failures generated by such practices and the range of policy responses thereto.

THE NEED FOR A NEW INSTITUTIONAL BALANCE IN DECISION-MAKING

The balancing of the above-listed policy tensions suggests that any fundamental changes in policy regarding the identity of those regulated and the nature of what is regulated should also bring about at least two fundamental changes in the manner in which the different institutional stakeholders cooperate in the enforcement process.

First, while European case law in the form of the Deutsche Telekom, Telefónica and TeliaSonera cases, among others, has clarified the residual role which competition rules play alongside sector-specific regulation in the EU legal order, it is also the case that the two disciplines often take approaches which at times contradict or compromise one another.[19] At a minimum, the approaches are not synchronised, so that decision-making occurs under different timeframes. Moreover, decision-making under the regulatory framework is very much centralised in terms of the veto power enjoyed by the Commission over many decisions of national regulators, whereas Regulation 1/2003 establishes a framework which decentralises decision-making in the implementation of competition rules.[20]

In addition, the introduction of Regulation 1/2003 has meant that settlements (similar to a US consent decree) now provide an alternative means of settling an access dispute, which means that ex-post access remedies now have the potential to be more effective and detail-oriented than their pre-2003 counterparts (ie. a year after the EU regulatory framework was introduced).[21] Most importantly, a series of merger decisions adopted by the Commission over the past few years, all of which have involved significant access obligations and spectrum divestitures, have drastically changed the face of the competitive landscape in many EU member states. The remedies adopted in those merger reviews are often more intrusive than those adopted under ex-ante intervention.[22]

Also, the use of the sector inquiry tool in relation to a number of problematic telecoms markets has meant that policy lessons have been cross-fertilised across the ex-ante/ex-post divide in relation to those affected markets. Finally, it is also true that there has been an increasing consolidation of regulatory and competition tasks among national regulators over the past few years (the Netherlands' ACM and Spain's CNMC are perhaps the most prominent examples), which means that the adaptability of regulators to work across disciplines is enhanced.

As a result of these developments, one must ask the question seriously as to why the time is not ripe for a radical overhaul of the ways in which the enforcement of the ex-post and ex-ante disciplines complement one another. In my view, an integrated approach is in all likelihood beneficial, and is arguably the most robust solution when one is pursuing so many overlapping (and at times conflicting) policy interests.

> **"There has been a yawning chasm between the Commission and national regulators."**

Second, there has existed for many years a yawning chasm between the degree of responsibility exercised by the Commission in its decision-making powers under its Article 7 powers of review, on the one hand, and national regulators when adopting decisions under the existing EU regulatory framework.[23] The former's veto decisions under the regulatory framework (which are in any event, rare) are assessed under the lower standard of review of 'manifest error' before the General Court in Luxembourg, while the latter are assessed according to the much higher standard of review 'on the merits' before the national courts.

In addition, there are very significant differences in the ways in which member state courts accord legal value to the opinions of the Commission – of which they must take 'the utmost account' – when the Commission expresses its views on the appropriateness of remedies adopted under the Access Directive.[24] This is because each EU member state has a different legal tradition as to how it will respect Commission opinions which do not have the force of law (because no Commission veto power exists with respect to the issue of remedy selection). To complicate matters further, both BEREC (the body representing European regulators) and the Commission must accord to one another due deference by again taking 'the utmost account'

of one another's opinions; in the absence of such a phrase being imbued with any legal significance at the level of Community law, the institutional dynamic has become unwieldy and its decisions have not carried the force of legal certainty in many jurisdictions.

As a result of these trends, the current process of decision-making is proving to be unsatisfactory since the inception of the EU regulatory framework in 2002. This has led to great uncertainty at member state level as to whether or not the decisions of national regulators could be vulnerable to challenge depending on whether or not they differed in their views from the Commission in the application by the latter of its own 'soft law' instruments and in the exercise of its discretion. Accordingly, in the wake of any revision of the EU regulatory framework, serious consideration has to be given to redressing the current institutional shortcomings which characterise decision-making by the three institutional stakeholders under the framework – namely, the Commission, national regulators and BEREC. Decision-making should arguably be more consensual earlier in the decision-making process, while the confrontational aspects of the Article 7 review process need to be avoided.

As noted above, the greater complexities of the marketplace and the sweeping nature of technological change also create greater pressure for a more flexible approach to be adopted towards enforcement which is reflected in fundamental competition law principles. There is a concern that substantive changes in the analytical elements of the framework will be vulnerable to ineffective implementation to the extent that existing institutional shortcomings are not addressed.

CONCLUSIONS

The review of the EU regulatory framework for electronic communications which is to take place later this year will need to address the policy trade-offs discussed above. In doing so, it will be important to acknowledge that the very successful regulatory model introduced in 2002, while still analytically coherent today, requires a helping hand if the future of a robust electronic communications sector in the EU is to be ensured.

The discussion above suggests that the regulatory framework that we should be implementing by the year 2020 should at the very least be sensitive to striking a balance between:

- The encouragement of network-based competition in urban areas, while ensuring an access option in rural areas
- The need to ensure open network architecture for future access against demands for more mandated access options
- A minimisation of ex-ante asymmetric regulation, while being responsive to competition law 'regulation' through merger reviews and settlements
- Flexibility to address emerging market failure problems from upstream or downstream elements of the internet value chain
- Greater legitimacy and flexibility in decision-making achieved through European Commission/BEREC cooperation at an earlier stage of the regulatory process.

> **Policymakers should not be satisfied with success with only a handful of policies.**

Achieving all of these aims will be anything but a straightforward task. However, the adoption of a holistic approach suggests that policymakers should not be satisfied with success with respect to only a handful of policies. The inter-relationships between the various policy strands suggests the opposite – namely, that a successful overall strategy is one which seeks to revisit all the lessons learned from commercial, regulatory and institutional developments since the adoption of the regulatory framework in 2002.

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REFERENCES **1** For example, see BEREC (2015). Report on oligopoly analysis and regulation, and Commission cases M.7217 Facebook/WhatsApp and Case M.6281 Microsoft/Skype. **2** For example, see case 7612, Hutchison 3G UK/Telefónica UK. **3** See directive 2014/61/EU on measures to reduce the cost of deploying high-speed electronic communications networks, pp1–14. **4** See Cave M (2014). The ladder of investment in Europe, in retrospect and prospect. Telecommunications Policy 38: 8-9. The objective of the framework is to provide new entrants with the opportunity to offer their services initially via the infrastructure of the existing operator. As a result, the revenue generated by new entrants should allow them to effectively 'climb the ladder of investment' and so have the eventual ability to be able invest in their own network infrastructure. **5** See the Access to Infrastructure Regulation provisions of Australia's Competition and Consumer Act 2010, which subjects networks deemed to qualify as essential facilities to a specific access regime overseen by the country's competition regulator, the ACCC. Recent considerations for the amendment of these provisions have concluded that an ACCC declaration designed to ensure network access to third parties should only occur when the grant of access would be in the public interest. **6** The conditions for a bottleneck are met when: (i) a facility is necessary, ie. if no second or third such facility exists (no substitute); and (ii) the facility cannot reasonably be duplicated as a way of controlling the active provider, ie. no potential substitute. See pp7-8 of the Commission recommendation of 9 October 2014. bit.ly/28PfqUw **7** The test considers dominance as only one possible cause of a significant impediment to effective competition, and thus 'widens the net' to catch a number of different situations. See Article 2(3) of Council Regulation (EC) No 139/2004 of 20 January 2004 and cases in note 2 above. **8** See directive 97/33/EC on interconnection in telecoms with regard to ensuring universal service and interoperability through application of the principles of open network provision. **9** See Alexiadis P (2015). Policy options for a revised EU access and interconnection regime. Digiworld Economic Journal 98 Q2 pp2-28. **10** See, for example, the relevant provisions within the Access Directive and directive 2014/25/EU on procurement by entities operating in the water, energy, transport and postal services sectors. See also the position within France with regard to mandatory open deployment of in-house wiring (one fibre line is deployed from the distribution point to each premises). **11** See Ofcom's strategic review of 2004 and the view that functional separation of BT has secured substantial improvements in the UK's fixed line sector, and the current strategic review. **12** See case M.7217 Facebook/WhatsApp and case M.6281 Microsoft/Skype. See also the CERRE study, Market definition, market power and regulatory interaction in electronic communications markets, especially chapter 8, and WIK-Consult (2013). The regulation of voice over IP (VoIP) in Europe. p3. **13** The UK Competition and Markets Authority published a report, The commercial use of consumer data, in June 2015, while the European Commission and Germany's Federal Cartel Office have begun to consider the issue in the context of their investigations into both Google and Facebook. The French and German competition authorities have also announced (at the end of 2015) reviews of the significance of big data. **14** Currently defined under Article 2(a) and 2(b) of the Framework Directive. **15** See regulation (EU) 2015/2120 laying down measures concerning open internet access and regulation (EU) 531/2012 on roaming. **16** For example, margin squeeze cases brought under Article 102 TFEU have adapted the use of LRIC cost models as a common requirement of 'cost', while the TeliaSonera precedent (case C-52/09) clearly establishes the principle that an ex-ante obligation to supply presupposes the need to supply an ex-post context. **17** Refer in particular to the language of Recitals 7 and 8 of the TSM regulation. By contrast, the Telecommunications Regulatory Authority of India (TRAI) took a restrictive position on zero-rating services on 8 February 2016, as have certain EU member states (Netherlands, Norway and Slovenia) prior to adoption of the TSM regulation. **18** Over the years, sector inquiries have been held in areas as varied as telecoms, such as the local loop in 2004, leased lines in 2002 and in 2000 for roaming. **19** Alexiadis P (2012). Balancing the application of ex-post and ex-ante disciplines under community law in electronic communications markets: Square pegs in round holes? In: Buttigieg E. Rights and remedies in a liberalised and competitive internal market. **20** Council Regulation 1/2003 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty. **21** See Article 9 (commitments) of Regulation 1/2003, pp1–25. **22** More details in: Alexiadis P (2015). Merger control in regulated sectors: A bridge too far? In: Ian S Forrester, A Scot without borders. Liber Amicorum vol II. **23** See Articles 4 and 7 of the Framework Directive, which are designed to ensure the accountability and independence of national regulators. **24** Although Article 4(3) of the TFEU expresses that member states' courts should take 'the utmost account' of the Commission's opinions, acts, or other forms of 'soft law' instruments, there is no obligation on the courts to interpret those instruments similarly or to achieve effective harmonisation along interpretational lines (also they may not be able to legally).