Body of European Regulators for Electronic Communications

BEREC

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BEREC Report of the Consultation on the draft BEREC report on Co-investment and SMP in NGA networks

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This document contains BEREC's report on the outcome of the public consultation on the "Draft BEREC report on Co-investment and SMP in NGA networks". Interested parties were invited to comment on the Draft. The consultation was open from the 9th of January 2012 to the 10th of March 2012. The Consultation Report summarizes by topic the main comments received and outlines how the BEREC plans to take into account those remarks in the final document.
12 contributions were received from the following respondents:

- British Telecom
- BUGLAS[1]
- Cable Europe[2]
- Deutsche Telekom AG
- ECTA[3]
- ETNO[4]
- FTTH Council Europe
- NetCologne
- Telecom Italia
- Telefónica
- Vodafone
- WIND

The following summary is not exhaustive. This document addresses the most commonly mentioned inputs. But BEREC would like to emphasize that all the inputs are duly taken into consideration and where possible have been used to improve the report.

[1] BUGLAS is the association of German telecommunication operators, which are planning, constructing and operating optical fibre networks. BUGLAS' associate members are providers of technological components, content and consulting services.
[2] Cable Europe is the trade association that groups all leading broadband cable operators and their national associations throughout Europe. The European cable industry provides digital TV, broadband internet and telephony services to more than 70m customers.
[3] European Competitive Telecommunications Association is an association which supports the regulatory and commercial interests of new entrant telecoms operators, ISPs and suppliers of products and services to the communications industry. The association represents the telecommunications industry to key government and regulatory bodies and maintains a forum for networking and business development.
[4] European Telecommunications Network Operators' Association, principal policy group for European electronic communications network operators

1. Introduction

The deployment of NGA networks brought along new issues related to market definition, the designation of operators with significant market power (hereinafter referred to as "SMP") and regulatory obligations. In the recent round of market analyses, and taking into account the NGA Recommendation published on September 2010, some Member States proposed to exempt fibre-based networks from specific obligations based on their early stage of development. However, a number of issues in this regard are likely to rise soon, as NGA development progresses.

Although co-investment can be a positive mechanism for stimulating investment in certain circumstances, depending on the characteristics of the arrangement between the co-investors, the scheme can result in situations that are close to a monopoly or situations that are close to competition if the agreement can ensure efficient competition and grant partners sufficient independence.

BEREC has published in December 2011 a draft report aimed at suggesting elements to be examined and specific sets of conditions and criteria considered to be suitable indicators of effective competition to national regulatory authorities (hereinafter referred to as "NRAs") facing NGA co-investment agreements in their national market and conducting the next round of market analyses of markets 4 and 5.

This draft report was submitted to public consultation from December 16th, 2011 to March 10th, 2012. The following documents summarise the main comments received by BEREC, as well as the subsequent amendments to the draft report BEREC made taking the utmost account of the respondents' views.

2. General comments

General approach of the draft report towards co-investment

Many stakeholders [BUGLAS, ETNO, FTTH Council, NetCologne, Telecom Italia, Telefónica, Vodafone] expressed that the general stance of the draft report was not positive enough towards co-investment. Respondents estimated that BEREC should consider co-investment as a pro-competitive tool, which enables non-SMP operators who could not realistically undertake deployment on their own to invest, rather than like a threat to competition and opportunity for collusion.

BUGLAS and Vodafone remarked that although the draft report generally acknowledges the possibility of a positive impact of co-investments on competition, this is not sufficiently reflected in the conclusions.

Some of the stakeholders [Telefónica, Vodafone] indicated they are especially concerned by the signals the draft report gives to potential co-investors, as they felt it encouraged them not to invest and rather wait, as their investment will become regulated if they associate with an incumbent. Those stakeholders invited BEREC to take a more neutral stance to avoid co-investment being hindered by regulation.

A negative stance towards co-investment was not intended by BEREC. To make this clear several changes of the wording throughout the report have been adopted.

Geographical segmentation

Several stakeholders [Deutsche Telekom AG, ECTA, ETNO, Telecom Italia, Telefónica, FTTH Council] pointed explicitly to the importance of geographical segmentation analysis of competition.

BEREC agrees and stresses this point in paragraph 1.1.4 of the report stating that the geographical market definition is an inherent part of any market analysis.

Respondents estimated that an approach that wrongly defines the market as "nationwide" risks diluting the actual competitive impact of alternative networks, and that only a regional segmentation of the markets provides an accurate assessment of competition.

They particularly pointed out that a regional segmentation allows for a better grasp of the respective market players' behaviour and incentives (including local operators), and thus of the market competitive conditions. In this regard, some respondents explained that the indirect effects of cable-based products on the behaviour of network operators at the wholesale level are better analysed from a regionally-segmented market than from a national market perspective.

BEREC has addressed this point already in the report. An additional paragraph on page 31 emphasises that the analysis may lead to different results according to the chosen perspective.

National / regional specificities

Some of the respondents [ETNO, FTTH Council, Telefónica] stressed the importance of taking into account national / regional specificities when applying a regulatory framework, and invited BEREC to avoid fostering a one-size-fits-all model of co-investment regulation as new co-investment schemes may still be created in Member states where few NGA rollout has occurred to date, in response to the varied nature of market competition across Europe. In particular, some respondents remarked that the number of players in the co-investment schemes that is fostering effective competition in an area might not be relevant in a different area with a different market structure.

BEREC agrees with this comment, which is fully in line with the report.

Scope of the report

Telefónica and WIND pointed out that the case of co-investment without the incumbent was missing in the report and that it should be included. WIND commented that, in case the incumbent is outside the scope of the co-investing agreement, it might still be able to influence deeply the behaviour of the co-investing party.

BEREC agrees with this comment. This report is however focussing on agreements with the incumbent. (see p. 15)

The FTTH Council believes a second report on co-investment is required, in order to go beyond the consideration of the impact on SMP coming from co-investment agreement and consider other factors such as the merits of co-investment in terms of accelerating investment and the role that NRAs can play to facilitate co-investment agreements.

Remedies were mentioned by a few respondents [FTTH Council, Telecom Italia, Vodafone]. Accordingly, Telefónica and Vodafone considered that it was unfortunate that remedies were out of scope for this report, which could provide guidance on how remedies might be structured in a co-investment scenario.

BEREC understands the relevance of these two comments, but the mentioned issues are out of the scope of the current report.

3. Regulation's intervention on co-investment

NRA's role in the definition of co-investment models and Open Access

On the one hand, some respondents [FTTH Council, Vodafone] expressed the wish to see the BEREC design co-investment models to give more guidance to the stakeholders, e.g. regarding the market shares of the operators involved in the co-investment, the favoured structure, possible arrangements regarding for example minority investor protection.

Vodafone therefore insisted the draft report should give clearer guidance on the particular circumstances under which co-investments can be assumed to lead to competitive wholesale markets and their impact on the market.

The FTTH Council also argued that NRAs should use their experience to set up an appropriate and functional design. Therefore, it encouraged BEREC to determine a desirable co-investment structure and encouraged NRAs to actively facilitate such an outcome.

On the other hand, other respondents indicated the role of NRA should be limited in those early stages of NGA deployment.

Some of the stakeholders [BULGAR, Deutsche Telekom AG, ETNO, NetCologne, Telefónica] argued that given the few co-investment agreements reported to date, co-investment models should still get a chance to develop freely and to be tested by the markets before undergoing normalisation through regulatory intervention.
BUGLAS and NetCologne highlighted that alternative co-investment models may develop under different regional circumstances, and this should not be impeded by premature regulatory intervention. They therefore warned against what they considered a premature setting of criteria, and wished the role of NRAs would be restricted to cases of market failure.
In a similar fashion, WIND suggested that the role of NRAs should be limited to a case by case analysis and to strong bottleneck cases, like the French model giving access to the in-house wiring.

According to Vodafone the cited Oxera report sees co-investments as a compromise between regulatory holidays and short term regulation.

BEREC is of the opinion that at this stage it is too early to develop detailed criteria. This BEREC report aims only at providing general guidelines.

Some respondents [BUGLAS, Deutsche Telekom AG, ETNO, NetCologne] pointed out that Open Access was not mentioned in the draft report, although it constitutes an important and possible scenario that can contribute to investment and competition.
They also stated that when Open Access agreements are successfully implemented, it may solve potential competition concerns otherwise addressed by regulation. Respondents

encouraged BEREC to include such voluntary Open Access models within the list of elements to be considered in the assessment[5].

BEREC agrees with this comment and addressed the topics voluntary open access and functional separation in two new paragraphs on page 54.

Co-existence of *ex ante* regulation and cartel law

Some respondents [BT, BUGLAS, NetCologne, Telecom Italia, Telefónica] stated that the existent framework (Cartel law) is enough to deal with co-investment and preserve actors independence. They recalled that co-investment assessments are subject to the monitoring by cartel law, and that non-discrimination and transparency obligations are also available in cartel law.

Therefore, some stakeholders [BUGLAS and NetCologne] estimated that additional regulatory guidelines were not necessary at this stage, as an adequate regulatory framework for dealing with broadband co-investment was already available. Telecom Italia added that, for now, an *ex ante* evaluation of the co-investment agreement's conditions cannot be considered justified and represents intrusive regulation.

However, BT indicated that, should co-investment occur in the UK, such arrangements should not reduce regulatory obligations where SMP operators are involved, nor should co-investment agreements overrule competition law.

BEREC agrees with these comments and clarified its position by restructuring the paragraph about competition law perspective.

Competition law and joint dominance criteria

Vodafone considered that joint dominance should be addressed in the report, as according to Vodafone the NRA would, in a SMP analysis in a joint-venture scenario, need to consider if the co-investors present themselves on the market in a co-ordinated manner or if there is effective competition between them, and it would need to show that the market fulfilled the so called **Airtours** criteria: market transparency, a credible retaliation mechanism and an absence of countervailing forces outside the jointly dominant firms (eg. buyer power, new entry or close substitutes).

BEREC has added a paragraph underlining the importance of the so called Airtours criteria for assessing joint dominance in the report on page 7.

Level of intervention

[5] BEREC further understands that a NGA Forum was held in Germany in October 2011[5], where the participants (telecom companies, energy companies, municipalities, associations) emphasised the need of voluntary Open Access products. Although they agreed on the need for voluntary access on a reciprocal basis, the participants did not reach consensus on the specifics of such agreements, such as the minimum amounts of access products or price setting. Non-discrimination and transparency were deemed of fundamental components in an Open Access concept, and standardisation of interfaces and processes have been assessed to be necessary.

Many comments were received with regards to the level of intervention [Cable Europe, Deutsche Telekom AG, ETNO, Telefonica]. The respondents felt the draft report generally encouraged co-investment projects offering wholesale access on layer 1 (ULL).

Deutsche Telekom and ETNO indicated BEREC should rather favour a neutral approach as indicating a preference towards co-investment projects offering wholesale access on layer 1 would potentially lead to inefficient network architectures, the costs of which would have to be borne by the end customers. Deutsche Telekom and ETNO considered the appropriate network access point can vary.

Only Vodafone indicated it does not find infrastructure-based competition efficient because of duplication, and warned against the dangers of wholesale and retail co-ordination via a co-investment vehicle.

Regarding the efficiency of infrastructure-based competition, BEREC has included a quote from the NGA Recommendation that specifies that NRAs are to promote competition in the provision of electronic communications networks, electronic communications services and associated facilities and services, inter alia, by encouraging efficient investment in infrastructure (paragraph 3.2.1.).

Although several players [Cable Europe, ETNO, FTTH Council] recognised the benefits of infrastructure-based competition, they commented that the scope for it should not be prejudged in advance. According to them, regulation should therefore refrain from imposing a general physical fibre unbundling obligation and should rather encourage infrastructure-based competition where it is feasible by leaving all possibilities open for as long as possible.

BEREC points out that the evaluation of remedies is out of the scope of this report.

Technical Neutrality

Most respondents [BUGLAS, Deutsche Telekom AG, ECTA, ETNO, Telecom Italia, Telefonica, WIND] argued that regulation should not try to influence or determine technology choices but rather support the market's choice of the most appropriate and efficient high-speed services. They therefore asked BEREC not to favour “multi-fibre” roll-out models over other types of approaches because different roll-out scenarios are appropriate in different market situations. They pointed out that favouring a single solution would probably lead to over- or underinvestment and to suboptimal results in the market in terms of infrastructure competition and innovation.

The respondents generally agreed that multi-fibre has some positive competitive properties, but they pointed out that BEREC should limit the draft report to state the pros and cons and take a neutral stance with respect to the available technologic solutions.

BEREC is of the opinion that this issue of a neutral stance with respect to technological solutions is sufficiently addressed in the report on page 43 and therefore only a slight changing of wording according to FTTC roll-out had to be added.

4. Characteristics of co-investment

Type of contract and risk sharing models

In the view of ECTA geographical swaps are not co-investments but merely mutual access agreements. In ETNO's view co-investments are risk sharing models that should include also volume commitments, upfront payments and non-linear access prices in general.

BEREC wants to emphasise that joint ventures and IRUs are the main types of horizontal agreements represented in the Member States to day. However, BEREC included an additional paragraph on page 33 mentioning other similar models that could also be examined by NRAs on a case by case basis.

Several respondents [Deutsche Telekom AG, ECTA, ETNO, Telecom Italia, Vodafone] indicated they believe that the legal forms of co-investment agreements doesn't necessarily have an impact on competition. They also advocated a neutral approach for the draft report leaving commercial players to choose the best option to fit their country/company case between joint-ventures or long-term agreements.

BEREC does not agree with these comments as joint ventures can only be regarded as equally favourable to competition as long term IRU agreements under particular circumstances and in the most favourable cases. BEREC understands that IRUs effectively define separate economic property rights associated with certain parts of the asset, allowing each IRU-owner to operate in full independence with respect to the use of its share of the asset. This structurally allows the IRU-owners to act as if they each owned an independent asset. By contrast, a joint venture is structurally the legal vehicle for a joint asset, which is jointly managed under a common strategy.

This said, these consideration cover exclusively the competitive aspects. BEREC does not express any preference regarding possible co-investment models.

A recent study by Oxera for Vodafone[6] discusses how a joint venture could be designed in such a way as to reduce to a minimum its incentives to discriminate between co-investors and competitors, without transferring IRUs. BEREC appreciates that the report provides useful information on techniques that could mitigate some risks for competition. However, under the proposed model, the co-investors would still have a joint interest in the co-financed asset (NetCo) and would only be prevented from discussing discriminatory strategies by multiple behavioural devices, rather than by incentives embedded in their property rights.

Vodafone added that rather than favouring the IRU model over joint-ventures due to the potential competition problems, the report should indicate concrete steps that can be taken to overcome those potential issues.

The BEREC report should at this stage only give general guidelines. Therefore concrete steps to be taken cannot be indicated.

Type and number of players

Regarding the type of players, Deutsche Telekom AG and WIND supported BEREC's perspective that the nature of the players of a given NGA co-investment agreement may have a significant impact on the assessment of SMP by the NRA. Deutsche Telekom AG recommended that when assessing the existence of SMP, NRAs should put a greater focus on the type of players included in the co-investment agreement and the conditions agreed between them, than on the legal form of cooperation chosen by the parties.

[6] Oxera (2011), *How a co-investment model could boost investments in NGA networks*, study commissioned by Vodafone, November, 110p. http://www.oxera.com/main.aspx?id=10069, retrieved on 5 April 2012.

WIND insisted on the need to evaluate carefully the different role of co-investors because their presence does not always improve the competition level among subjects involved in the same market. The stakeholder recommended paying particular attention to the SMP operator, namely their nature as a public company or as a financial investor or even as a utility company, because it can influence the competition level. Finally, WIND considered that co-investment agreements involving utilities company that do not operate in the telecoms markets, (retail or wholesale), introduce further complexity in the evaluation of the competitive impacts of the agreement itself.

BEREC already referred to different roles of co-investors in its report (see page 7).

For the case of one of the players being a public fund, the FTTH Council highlighted that significant public funds can be potentially distributed using co-investment models to reach areas where competition cannot reach commercially.. On the same matter, WIND warned that agreements involving public entities should be guided by a principle of transparency, more than in case of agreements that does not involve a public entity.

Regarding BEREC's assessment on scenarios where a small number of partners are parties to a co-investment agreement, BUGLAS pointed at that in practice co-investments with only two partners are likely to be the rule, as co-investment agreements between two partners already involves significant efforts, costs and risks. BUGLAS considered that if NRAs discourage co-investments with a small number of partners, then broadband deployment in rural areas could be impeded.

Independence of participants and new entrants

Some of the contributions [Telecom Italia, ECTA, Vodafone] underlined the importance of the independence of the partners, and recognized it was addressed in the draft report.

However, Vodafone expressed the wish for the draft report to detail the evidences needed to determinate whether the co-investment partners as independent players or a single entity, as this will then determine whether a single or joint dominance case has to be considered.

The FTTH Council believes that any co-investment implies a high degree of vertical separation between business units with consequences for market dynamics and the consequent regulatory obligations.

ECTA felt the draft report should further clarify and include in its conclusions that later entrants and third party access conditions to the co-investment venture are important in assessing the extent to which co-investment arrangements are pro-competitive or lock in a narrow oligopoly. ECTA distinguished between third parties accessing the jointly-built infrastructure and third parties entering the co-investment agreement at a later stage.

According to Telecom Italia, there is no risk of discrimination in a co-investment agreement since the conditions are freely negotiated among the parties and each operator entering into the agreement can decide not to participate in the investment if it finds the conditions not to be satisfactory.

BEREC added a new paragraph to explicitly address access to late entrant on page 53. This new paragraph focuses firstly on access conditions to the commonly-built infrastructure for third parties, and secondly on the access conditions to late entrants in the co-investment agreement.

ECTA acknowledged that the conclusion to the report identifies some of the relevant factors, which might reinforce the independence of participants to the co-investment vehicle and lower entry barriers but considered that would be helpful to identify the optimal factors which combined would tend to improve competitive conditions in the market.

The BEREC report should at this stage only give general guidelines. Therefore concrete steps to be taken cannot be indicated.

Functional separation and information exchange

BT noted that an eventual functional separation of the incumbent or other operators needs absolutely to be considered in an SMP analysis. Moreover, Vodafone noted that given the particular concern over information-sharing highlighted in the report, it would be useful if it could give concrete examples from the well-known cases of functional separation such as BT to demonstrate how the risks of co-ordination can be minimised. According to Vodafone, the report should highlight these best practices and describe how they could reassure an NRA that co-investors should still be considered competing entities in a particular market.

BEREC agrees that functional separation should be considered and has added a new paragraph on page 54.

Risk sharing: compensation mechanism

Most comments [ETNO, Telecom Italia, Telefonica, Vodafone] regarding compensation mechanisms indicated that ex ante restriction on compensation mechanisms may prove counterproductive.

ETNO estimated BEREC should stay open to diverse risk-sharing models. The respondent agreed BEREC's view regarding the importance given to having an appropriate definition of property right to control transaction cost and market competitiveness.
ETNO also stated that risk sharing through long-term pricing agreements coupled with risk premium can be a solution to ensure a level-playing field between investing and non-investing market players.

Telecom Italia suggested that network access should be granted also to parties not participating in the co-investment on the basis of not discriminatory and fair prices. Telecom Italia added that the risk sharing does not eliminate the investment risk so a risk premium is to be provided for also in co-investment agreements.

BT noted that BEREC should define the acceptable level of risk premium from with co-investing parties can benefit and make it clear that no other form of discrimination between co-investors and third parties should be permitted.

Transparency

BUGLAS and NetCologne stressed that the draft report should insist on transparency and non-discrimination and let market force operate. The respondents added that an essential regulatory task regarding the NGA rollout is establishing transparency and non-discrimination for all market players. They estimated that BEREC should intensify its support towards a more competition-enhancing way through the removal of information- and access-bottlenecks and the establishment of the required transparency regarding network modification plans of SMP operators.

Telefónica pointed out that BEREC should ensure regulatory certainty to encourage investment and the stakeholder expressed concerns about the part mentioning “asymmetric forms of regulation” which could reduce incentives to invest

WIND felt that detailed rules of transparency for co-investment agreement involving a public entity should be defined, and that the evaluation of such agreements should be conducted through a public consultation involving all the relevant stakeholders.

BEREC will include transparency and non-discrimination in paragraph 3.4.1.