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**Introduction of competition in the communications market**

**- The European Experience**

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## 1. INTRODUCTION

Let me thank the organisers for the opportunity to speak at this panel on the European experience in the liberalisation of the telecoms sector, at a time when telecommunications in this country moves into a new decisive phase of liberalisation.

I would like to concentrate during this talk on three areas:

- ◆ The European experience three years after full and unlimited liberalisation of the EU's telecoms market on 1<sup>st</sup> January 1998 and some lessons that may be drawn;
- ◆ The new concepts published last year for further reform that should take account of the future convergence of the telecom—Internet—media markets;
- ◆ The key role that content now plays for the development of the electronic communications sector, as a main driving force of the future broadband platforms.

## 2. THE EU TELECOMS LIBERALISATION PROCESS

Let me first look at the situation three years after full liberalisation in the EU of all telecommunications services in 1998—fixed, long-distance, and local, as well as mobile.

The EU process of liberalisation was a process in successive stages, not dissimilar to the process in this country that is also progressive.

The EU process started in 1987 with the basic EU Green Paper on telecoms that foresaw at the time full liberalisation of equipment, terminals and value-added services. The subsequent legislation set a timetable for reviews for further liberalisation.

These reviews led in 1993 to the decision to fully liberalise *all* services—local, long-distance, international, and all networks, by 1<sup>st</sup> January 1998, and a decision to design and put into force by that date a regulatory framework for *unlimited* market entry.

Some of the 15 EU Member States obtained slight extensions of the liberalisation deadlines: Spain 11 months, Portugal 2 years, and the last deadline ran out for Greece by the end of 2000.

In preparation for the liberalisation deadline, privatisation of the public carriers started massively during the second half of the nineties, and was substantially progressed by the year 2000, even if Member States' governments still have important share holdings in a number of incumbent carriers.

Building on the Information Society concept that had been developed in the EU during the mid-nineties—along similar lines as in the US—the EU started by the end of the nineties a convergence debate that resulted *in a new reform package* submitted in July 2000 to the legislative process. The new reform is intended to adjust the European regulatory framework to the convergence of markets and to the wider goals of the e-Europe programme for the Internet and e-commerce, as announced at the 2000 Lisbon and subsequent European Councils, the meetings of the European Heads of State.

### **3. THE EUROPEAN VS THE US APPROACH**

The EU framework of Directives for full liberalisation on 1<sup>st</sup> January 1998 basically compares with the US Telecom Act of 1996 that liberalised, in principle, fully US telecoms. But the European framework was developed against a different background.

The US telecom scene, after its initial phase of liberalisation of terminal connecting equipment and value-added services — or in the terms of the Computer I and II inquiries of the late seventies and early eighties "enhanced services" — was deeply marked by the AT&T consent decree, and the subsequent splitting of the Bell system of the time into local and long-distance companies. The resulting dichotomy of the US telecoms sector into local and long distance dominated US regulatory thinking and debate for the period up to the 1996 Act.

Even if since the Act of 1996, the overall US agenda and the European Telecom Agenda look fairly similar—centring on issues like interconnection and access, universal service, treatment of the Internet—the post-1996 period is still substantially characterised by this structuring of regulation: for example by the strict link between competitive entry opportunities in local Bell Operating Companies areas with the possibility for those local companies to enter the long-distance market, and the numerous FCC and Court proceedings linked to that issue.

In the EU, we have not had the same heritage, and we have no basic regulatory distinction in the EU framework between long distance and local. We had a short debate in 1992 about liberalising long-distance voice only between Member States, but this was found to lead to complex problems, and therefore the decision was taken to liberalise *all* voice services within a single framework, with no lines of business restrictions for operators, except those that may result from general anti-trust law.

#### **4. WHERE WE ARE**

So, where are we in Europe? The European Commission issues each Autumn a report on the implementation of the liberalisation package of measures of the 1998 framework in the Member States that gives detailed information on markets, licence types, fees, number of operators, universal service performance, rights of way, etc. and bench-marks progress against EU objectives.

The report for the year 2000 and its detailed annexes are available on the EU web site ([http://www.europa.eu.int/information\\_society/topics/telecoms/implementation/index\\_en.htm](http://www.europa.eu.int/information_society/topics/telecoms/implementation/index_en.htm)) and I will therefore only mention a few figures that emphasise the main points.

The period 1998 - 2000 has been characterised by successful liberalisation and market restructuring of the European telecoms sector. The period was characterised by:

- ◆ Extensive liberalisation of markets;
- ◆ Rapid mobile expansion, substantially outpacing original forecasts;
- ◆ And—up to Spring 2000—by an Internet boom that brought substantial support by capital markets for the restructuring of telecom markets;
- ◆ National Regulatory Authorities (the NRAs) were established successfully in all fifteen Member States, interconnection regimes started to work and the foundations of the regulatory framework for the new competitive telecom markets were put in place. Growth accelerated to an average rate of 9% throughout the period;

- ◆ In the market for mobile services, penetration has gone up over the year 2000 from 36% to 55% (now 62%). There were 194 million subscribers to GSM services in the EU by the end of 2000, and 61 operators were licensed for the provision of digital mobile services (up from 52 in 1999);
- ◆ In the fixed market, according to the report, end year 2000 467 operators were active in the market offering public voice telephony services for long-distance calls (up 90% from 1999), 475 for international calls (up 70%), and 401 for local calls (up 80%), many of them offering all three services according to their choice. Carrier pre-selection was used by 180 new entrants for the provision of long-distance and international calls, and by 69 for the provision of local calls. 861 operators have been allocated access codes for the provision of voice telephony via carrier selection.

The extent of competition can be seen from the fact that on EU average 80% of EU citizens can now choose between more than five operators for long-distance and international calls, and 95% have a choice between at least two. 30% can choose between more than five operators for local calls and 45% have a choice between at least two. Prices for international and long-distance calls have fallen since 1 January 1998 by an average 35% and there is full possibility of choice in the field of mobile communications.

## **5. DETERMINANTS OF SUCCESS**

Though figures for 2001 will be marked by the end of the Internet boom and the effect of high licence fees in the European 3G process, the basic achievements are likely to be sustained.

Let me therefore have a look at the determinants of this success that also highlight main features of the current telecom regulatory framework in Europe.

Main determinants of success for liberalisation were:

- ◆ Public consultation and support;
- ◆ Firm date for full liberalisation;

- ◆ Creation of strong regulators for the sector.

### *Public consultation*

Public consultation and support have been the very basis of the progressive liberalisation process in the EU. It seems that we have followed here both in Europe and in this country similar avenues, with wide spread use of consultation and Green Books.

### *Firm date*

A decisive outcome of the debate in Europe was the decision to fully liberalise on 1<sup>st</sup> January 1998, without limitations on the number of market participants (neither in network infrastructure, nor long-distance, local, and international). Licences were to be limited only on the basis of scarce resources—radio frequencies, therefore for mobile—and, potentially, numbering, and other public requirements where Member States could justify limitations (such as safety, and town planning aspects).

After a long debate on the universality requirements for services, the European Union came to the conclusion that—under European conditions—the objective of universal service could be achieved by more proportionate means than entry limitations, such as by setting up of universal service funds financed on a shared basis by market participants. According to the European debate, the objective did not justify restrictions on the number of market participants or delay in market entry of competitors.

### *Strong regulators*

The EU framework was based on a set of EU Directives that left substantial margins for implementation to individual EU Member States. This has led to strong national regulatory authorities in the fifteen Member States. We have paid a price for that flexibility with sometimes substantial divergences between Member States (that are, in fact, criticised in the EU implementation reports). But at the same time a strong grassroots regulatory structure was created in the 15 Member States that is now the base of Europe's liberalised telecom market.

## 6. THE 1998 REGULATORY REGIME

These general orientations have translated in Europe over the last three years since full liberalisation in all fifteen Member States into a fine tuned regulatory framework that has led to:

- ◆ The creation of an operational interconnection regime across the EU, as the very basis of development in a liberalised market;
- ◆ The principle of proportionality as the basis for addressing the issue of universal service. I will say a few more words about this;
- ◆ An agreed framework for basic regulatory issues: licensing, interconnection, rights of ways, radio frequencies, numbering

Let me make some comments on each of these issues, and the basic principles applied:

### *Licensing*

Europe did not choose to follow the US model that had been dominated up to the Telecom Act of 1996 by long-distance competition and the maintenance of local monopolies. The distinction made under the European regime was between networks and voice services on the one hand (that are subject to individual licensing procedures under the current regime), and all other services on the other hand (that are subject to general authorisation/declaration schemes only). No regulatory distinction of principle is made between local and long-distance, or international.

In more detail, the current European licensing regimes are subject to the following main requirements:

- ◆ Individual licences only for public voice telephony or public networks, or for the use of scarce resources, i.e. radio frequencies (e.g. mobile services), or for imposing universal service conditions, competition safeguards, or certain essential or public interest requirements (defined in EU Directives);

- ◆ Procedures must be open, non-discriminatory and transparent, guaranteed by the regulators;
- ◆ Time deadlines for issuing licences: according to EU directives, six weeks as a standard, extended to four months under certain conditions;
- ◆ Fees should cover administrative costs for issuing licences only, or the need to ensure optimal use of scarce resources.

However, the latter allows also auctioning of radio frequencies—a procedure used extensively in the 3G-licence process in Europe, and leading to very high licence fees in some Member States, as is well known.

Services *not* included under the EU definition for the provision of voice telephony can only be subject to a light authorisation scheme. For example, call back will not normally be classified as an independent voice service and therefore will not be subject to licensing or declaration requirements. In Europe, the issues surrounding call back services and similar services have tended to become rapidly non-issues, given the substantial decrease in international tariffs on many EU international routes subsequent to full liberalisation.

This approach also means that Internet service providers are only subject to the light general authorisation regimes. Internet service providers therefore do not require individual licences, and the Commission has consistently stated that at this stage there will be no regulation of voice over the Internet and therefore no license requirement. Full competition in international was included in full liberalisation from the start, and has dramatically lowered international telephone rates for the European consumer. We have now reached U.S. levels for international calls. Competitive voice service providers are offering these routes for some 10 cents / minute, and below.

All of this rapidly generated substantial consumer benefits and brought citizens' support for liberalisation.



*Interconnection rates*

The establishment of an operational interconnection regime was the very basis for rapid development of competition after full liberalisation. The Commission continuously benchmarked national performance. Interconnection rates for local access have now decreased to below 1 cents/min.

*Carrier selection*

The European Commission singled out this area very rapidly for action and issued a Directive concerning call-by-call selection, pre-selection and number portability. These features turned out vital for rapid entry of competition in the long-distance and international markets. They were implemented in nearly all of the EU Member States by end 2000.

*Billing*

In a number of Member States regulatory requirements to allow access to the incumbents' billing system generated substantial consumer confidence by allowing integration of the competitor's long distance and international bill into the consumer's bill from the incumbent, substantially facilitating bill clearance for the competitors, but also re-assuring consumers.

*Two further comments: Universal service and rights of way.*

Universal service goals are the fundamentals of any telecommunications policy in any part of the world: in Europe, in the U.S. and, of course, in this country.

In Europe, it has turned out that competition, and the additional investments it brings, has not reduced but substantially increased universal service (that is defined in great detail in the EU Directives). The main effect of competition, or the threat of unlimited competitive entry, has been a substantial increase in the performance of the universal service providers—the incumbents. To date, only two Member States have used the safety net provided for in the framework to secure the financing of universal service deficit: universal service funds financed by market participants on a shared basis—as they also exist in the U.S.

Rights of way and sharing of ducts, antennae, and other facilities fall in the EU often under local authorities and municipalities' jurisdiction, and therefore seemed an intricate problem for infrastructure competition. The issue has been addressed in the EU framework by the strict application of the principle of non-discrimination with regard to the incumbent. Sharing has been allowed for where, for example, town-planning aspects limit availability of land and digging possibilities. While certain problems persist, most EU Member States seem to have addressed the issue successfully.

## **7. OVERALL BALANCE POSITIVE BUT SUCCESS IS BASED ON A FRAGILE BASE**

The basic scheme in EU regulation seems to have worked well: regulation concerning telephone prices, interconnection obligations, universal service, and cost accounting centred on operators with Significant Market Power (the incumbent); a lighter handed regime for new entrants.

The overall balance is:

- ◆ Introduction of competition was successful

But

- ◆ This applies mainly to long-distance, international, and mobile.
- ◆ The share of the incumbent ex-monopolists in the local market is still an average 95%.

This means that competition rests on very fragile grounds. By mid-2000 it led to the conclusion that the introduction of competition in the EU's telecom sector was successful but that new concepts were required. This re-thinking was also prompted by the new critical phase that we have entered:

- ◆ The set back in the capital markets due to the general dramatic drop in high tech stocks, once the Internet boom of 98/99 had collapsed;

- ◆ The high debt and interest charges resulting from the UMTS 3G license process in Europe;
- ◆ The resulting squeeze on the financing for new entrants. Market entry has become substantially more difficult.

## **8. THE CURRENT REFORM ADJUSTS THE 1998 FRAMEWORK TO THE NEW SITUATION**

This takes me to my *next* point, the current reform of the EU framework. Time allows only giving an outlook. In Spring 2000, the EU published its comprehensive eEurope plan that was confirmed by the European Councils of Lisbon and Feira, aiming at the development of Internet and e-commerce on a broad basis. Part of this plan was major reform of the 1998 telecom regulatory framework.

As published in July 2000, the “reform package” called for:

- ◆ Further opening of the local bottleneck;
- ◆ Regulation based more on market analysis, gradually moving away from regulating the incumbent towards developing a framework for the future telecom - Internet - media markets. In practice this means that the concept of electronic communications becomes the basis of regulation (instead of the current focus on the telephone voice service);
- ◆ As a consequence, a growing role for general anti-trust rules, in close interaction with telecom specific regulation.

The two responsible Commissioners have spelled this out clearly. European Commissioner Liikanen on the reform package:

- ◆ Simplify and clarify regulation;
- ◆ Adapt the 1998 framework in the light of technology and market development. This means principally taking account of convergence and therefore focusing attention on the new electronic communications framework.

Commissioner Monti on competition and regulation:

- ◆ In favour of the maximum application of competition law;

But

- ◆ Possible "need for regulation to extend to other areas where the competition rules are not yet effective".

These statements define the combined action of telecom regulation and general anti-trust action under EU Law.

The basic rationale of the approach is:

- ◆ Europe must open the competition in the local access markets;

And

- ◆ Flexibility in the application of telecom regulation must be developed further, in order to adjust more rapidly to new market situations. The main issue is moving away from the current focus on voice to a broader electronic communications perspective.

Main measures of the package were:

- ◆ The EU regulation of 18 December 2000 mandating unbundled access to the local loop in the EU as of 1 January 2001. This implies a mandatory requirement on the incumbent ex-monopolist to provide unbundling;
- ◆ A general reform of the 1998 Directives. This concerns the consolidation of the different existing Directives into a few core Directives, and adjusting them to the new focus on electronic communications and related market definitions.

## **9. COMPETITION IN LOCAL ACCESS MARKETS IS A CENTRAL GOAL**

The EU Local Loop Unbundling (LLU) Regulation mandates:

- ◆ Fully unbundled access to the local loop—the taking over of the full management of the incumbents' line by the competitor, including the management of the subscriber relationship;

And

- ◆ Shared access—this implies access to the non-voice frequency spectrum of the line only, essential for transmission of xDSL, without taking over the voice telephony subscription.

The *issue is not a choice* between unbundling of the existing local loop *or* building new alternative infrastructures.

We need both and these options are complementary. However, new entrants should have the possibility to combine both options to reach reasonable penetration of the local market within a reasonable time. This can only be done via opening the use of the existing local telephone wire—the network with by far the highest penetration in two-way communications in most countries. The balance between building of new infrastructures or buying use of unbundled network elements from the incumbent should be drawn by the new entrants, *not* the regulator and *least* the ex- monopolist.

In Europe, unbundling is seen as a means to substantially accelerate the deployment of xDSL (the various modes of digital subscriber line technologies). xDSL is seen to offer the potential for deployment of access to the Internet of a new dimension—high speed at flat rate via the normal telephone copper wire. xDSL means putting the telephone line to full use, across *its entire* frequency spectrum. It offers—together with the cable modem option, fixed or wireless—the chance to leapfrog into the next generation communications infrastructure.

We are still at the very start with unbundling in Europe, and the effect of the new unbundling Regulation has to be seen. But effective unbundling is a necessary requirement to ensure that the new markets have a chance to develop in a competitive environment. There remains the threat that the existing dominant positions in the local loop will be expanded into the new xDSL markets.

## **10. MORE EMPHASIS ON ANTI-TRUST CONCEPTS IN REGULATION**

The other main objective is adjusting the 1998 EU framework to market based regulation:

- ◆ The determination as operator with Significant Market Power (SMP) remains the basis of regulation;

But

- ◆ In the future, this determination must be made by the regulators according to determination of dominant positions based on the principles set by general competition law.

This should give the EU's regulatory framework more flexibility to adjust to the new situations as markets converge.

To summarise the content of the 2000 Reform Package, let me say the following.

The essence of the package is:

- ◆ More flexibility;
- ◆ Accommodating the convergence of markets;
- ◆ Integration of general competition law principles;
- ◆ Regulation focused on actual market situation.

The reform is necessary to introduce the new degree of flexibility that the rapidly moving markets require. However:

- ◆ Difficult issues of market definition are ahead, and;
- ◆ Market definitions will become key in EU regulation, as demonstrated by the publication of the Commission's guidelines on market definition and the calculation of significant market power earlier this year.

Re-centring regulatory systems on actual market analysis will not be an easy task. Issues are:

- ◆ Stability of market definitions;
- ◆ Coherence between regulators;
- ◆ Anticipation of future market developments.

All of this has become focus of attention in the regulatory debate in Europe over the last months, as the package progressed.

More generally, the new approach will mean more emphasis on general anti-trust principles:

- ◆ Re-definition of SMP (Significant Market Power) in terms of analysis of market power according to competition law principles;
- ◆ Continued intensive screening of mergers & alliances under anti-trust law;
- ◆ Intensified application of antitrust to access to content where competition law principles start to play a major role.

## **11. BESIDE LOCAL ACCESS, CONTENT BECOMES NEW CRITICAL BOTTLENECK**

Therefore, a few words on this last aspect I wanted to cover: the new critical role of access to content for the development of the converging telecom - Internet - media markets.

As new platforms for digital satellite, cable, and terrestrial television are introduced in Europe we find that premium content becomes the new critical bottleneck for successful introduction of any of the new platforms.

- ◆ Access to premium content is decisive for the new TV and video platforms;

- ◆ Access to sports rights tops the agenda;
- ◆ Availability of rights for distribution of content via broadband Internet and UMTS will be critical for rapid deployment of those new media.

The days where telecom systems and platforms could be deployed independently of access to content are coming rapidly to an end.

*No content means no successful market entry in many cases. It is premium content that gives the competitive edge. Future conduit cannot grow without that content and vice-versa.*

The issue is more and more at the centre of competition concerns for both telecom and media. It is in the media field that the two fundamental concepts of the future economy must find a new relationship: *the right to property and IPRs; and the requirement for access*. Competition law principles are bound to play a key role in developing this balance.

This gives a new key role for the application of competition rules to the sector. Let me quote Commissioner Monti: *"exclusivity for premium content of a long duration and for a wide range of rights is unacceptable because it is likely to lead to market foreclosure"*.

Access to content for the new platforms will be a focus of attention for both regulation and competition law enforcement in the European Union during the next months—and years—as will be the inverse problem of access to these platforms for content providers. And we will talk more and more about the new technologies that could become rapidly mainstream: UMTS, broadband Internet, and the many new forms of streaming, packaging and interactivity.

Without going further on this issue at a conference that is focused mainly on the conduit side, suffice it to point to this critical factor.

## 12. OUTLOOK

Let me end with a short look at the future of communications in Europe during the decade. The new markets will be:



- ◆ Internet broadband / new cable and satellite platforms;
- ◆ A key "enabler" will be market oriented regulation;
- ◆ Technologies are getting in place: xDSL, upgraded cable, upgraded wireless, and satellites;

And,

- ◆ A new bottleneck is shaping up: access to content.

A main test for regulation and competition law enforcement will be tackling in an efficient manner both: *the local access bottleneck, and access to content.*