

EUROPEAN COMMISSION

SECTOR INQUIRY

On the Competitive Provision of Leased Lines in EU Telecoms Markets

Public Hearing – 22 September 2000

Maintaining the Competitiveness of European Business: The Role of Leased Line Pricing and Availability

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Summary

In July 1999 the Competition Directorate-General launched an inquiry into leased lines as part of its sectoral investigation into telecommunications. Today we are here attending a public workshop to discuss the results of the investigation into the competitive provision of leased lines in EU Telecoms markets. INTUG has been calling for an investigation into this market since 1979, and congratulates the Commission on the thoroughness of the investigation so far. INTUG trusts that the outcome of the investigation will be that substantial steps will be taken to remove what we regard as anti-competitive practices in the industry.

Agenda

First let me say a few words about INTUG, and then why INTUG regards leased line pricing as important. I will then summarise INTUG's view of the current market, and comment on the issues facing the Commission.

The International Telecommunications Users Group (INTUG) was formed in 1974 after an European Commissioner complained that the Commission was deprived of telecoms user input as it could not treat with national user groups without treading on the corns of member states, and no international group existed. INTUG's first members were European national telecoms user groups and, although it later admitted multinational companies to Associate Membership, it has been careful to this day to ensure that the user groups, which form its Council, control its policies and actions. INTUG's associate members are multinationals to whom telecoms costs and services are important; they range across the financial, air transport, oil manufacturing and other sectors. Many of them run global data networks constructed using leased lines; for example Reuters spends over 5% of its revenues on leased lines.

INTUG Europe combines the European interests of the members of INTUG including national associations, corporations and individuals - telecommunications users across Europe. It represents the many thousands of telecommunications managers in businesses across Europe, from the largest corporations to small enterprises, who are purchasing and managing the company infrastructure on which are being built the new e-commerce and m-commerce applications.

Importance

The introduction to the Commission's report notes that the cost of access to the Internet is key to the growth of e-commerce in the Community; leased lines are the primary way in which medium and large businesses connect to the Internet. The Bangemann Report also noted the effect of leased prices on economic growth and innovation. The cost of ISP services is also highly dependent of leased lines, as ISPs use these to connect their sites together both nationally and internationally. Leased line prices are also key cost drivers for MNCs, as I mentioned earlier.

Market changes over last 5 years

In addition to issues surrounding the cost of leased lines within the EU, the international position is also a concern. The OECD, in its recent report (updated in June 2000) on local access pricing and e-commerce, suggests that there is a growing 'international digital divide' emerging between OECD countries. This conclusion is contrary to a widespread view that the gaps between countries in the development of e-commerce is narrowing. For example, the penetration rate of Internet hosts for the US in March 2000 was 7 times that of the EU. Internet users in the US have access to the Internet at higher speeds and lower prices, resulting in acceleration of the development and take up of e-commerce. One of the factors behind this is the pricing of leased lines in the US, particularly the cost and availability of high speed leased lines. In the New York area Reuters has found it cost effective to lease 622 Mbit/s SONET rings; in Europe the availability and of circuits at 34 Mbit/s and above is still very limited and the costs much higher than in the US. The UK regulator recently reported on leased lines after a study lasting most of this year, and although it concluded that prices were generally higher in the UK than the US, it did not find the differences as great as those experienced by Reuters and other MNCs. This is because deep discounting and one-off deal pricing is a standard feature of the US market; recently Reuters was receiving a discount of about 80% on national leased lines in the US. To redress these issues the key is the state of competition in the supply of leased lines in the EU.

In November 1995 the BTG, the Dutch business users association, invoked the conciliation procedure in the *Leased Lines Directive* (92/44/EEC). The dispute with PTT Telecom Netherlands (now KPN) concerned the tariffs for the national half circuit of international leased lines. BTG challenged the very high ratio between the tariffs for international and the equivalent national leased lines. It questioned whether cost-orientation had been applied to the tariffs for international leased lines, as was required in the Directive. The dispute was not unique to the Netherlands, with similar problems in all member states.

To support this, INTUG Europe undertook an independent survey of prices in the member states. This covered: analogue M1020 circuits, 64kb/sec circuits, 2 Mb/sec circuits and for the same distances nationally and to neighbouring countries within the European Union. It was modified in 1998 to reflect the changing market situation: analogue M1020 9.6 kbit/sec circuits were dropped and digital 34 Mbit/sec added.

INTUG's experience is that there is now a competitive market for 2Mbit/s international leased lines between the capital cities, and some other major cities, of Western Europe. Prices have fallen rapidly in the last 5 years - by more than a factor

of 10 on some routes, but continue to vary widely, in spite of the requirements of the leased lines directive. Within countries where competing carriers have built infrastructure, there is a competitive market for 2Mbit/s leased lines within and between major cities. However, both these markets are restricted by last mile access both in regards to cost and service quality.

The Commission has recognised the importance of short distance leased lines. Where the last mile of long distance leased lines is provided by former incumbents - multi-provider leased lines – the resulting lines are more expensive and have lower availability than circuits provided building to building by single carriers.

Outside major cities this situation is more acute; often the former incumbent is the only carriers who will quote for leased line provision, and there is no effective competition. Incumbents' prices for such leased lines are often double or treble the market price for similar distance end – to – end circuits from city to city provided by their competitors; from this we conclude that former incumbents are not trying to compete in the competitive city – city market; instead they are exploiting their near monopoly position outside cities to charge prices that are out of step with both the market and costs.

The slides show the difference between national and international lines and that 30% price differential target has been achieved in one EU country, but with little changes in others, where half circuits still cost over 5 times the national price. On short distance lines and 64k international lines, in some countries there have been negligible changes since 1992. On 2Mbit/s national lines, excessive prices have reduced, but some have barely changed at all, indicating that competition is not effective, in spite of the technological advance in optical fibre transmission.

For nx64kbit/s and high speed lines above 2Mbit/s we have found a less developed market. In some countries the national nx64k market has not been addressed by competitors, and prices have changed little in the last 5 years, whereas in other countries prices have fallen significantly. The market for 34Mbit/s and higher speed services is not well developed, with many suppliers quoting 'price on application' rather than publishing prices.

Key Issues

INTUG concludes from the above that it is premature to declare the total market for leased lines competitive; we should certainly await the outcome of the 2002 review. Declaring part of it competitive leads to the difficult question of market definition. There are many parts of London, Paris and Frankfurt not yet served by competing providers, hence even in the major cities we do not have a fully competitive market. OFTEL is planning to define a central London zone, where they consider the market to be competitive; our experience is that even in central London not every building is yet served by a competing supplier.

The key issues are:

- market definition

- geographic markets
- defining effective competition

As was made clear in our observations on the *Common Regulatory Framework*, the idea that a competitive market could be carved out of a national market is likely to have very unsatisfactory outcomes. It is the reverse of what is usually done in competition law, where a geographic market is defined in terms of an abuse of dominance in a market, rather than its absence. Before allowing part of a market to be designated competitive a full-scale assessment and consultation should be undertaken for the national or pan-European market by the NRA(s) concerned. At the least, such a separation of markets would add considerably to the complexity of determining and allocating costs.

Some capitals and other major cities, or at least their central business districts, could be argued to be competitive. However, that would leave other parts of the city and the rest of the country having something less than effective competition. It is not clear that it would be any more likely to become competitive as a result of segregating off the major cities. Indeed, it might very well slow down or stop that process.

It is conceivable that a market that has been designated as being competitive subsequently regresses to being non-competitive, i.e. that competition has not proved to be sustainable. In those circumstances it must be possible for regulation to be restored.

Recommendations

It has been suggested to us that it is likely that the Commission will propose to repeal the various leased lines provisions in Directives, once the corresponding market has been shown to be sufficiently competitive. INTUG regards this as premature for any speed other than 2 Mbit/s, as the competition in the nx64 kbit/s market is very limited. Even at 2 Mbit/s, it is impossible in our view to define precisely where the market is competitive and where it is not. On the contrary, INTUG proposes that the provisions of the Leased Lines directive needs to be extended to 34, 45, 155 Mbit/s and beyond, as price variation in this market is much greater than at 2 Mbit/s, evidence that incumbents' prices are not following cost oriented principles.

The importance of short distance leased lines to the development of a competitive market has been recognised by the Commission, which the introduction earlier this year of benchmarking; we applaud this initiative, and recommend that benchmarking be extended to all distances and speeds.

In the *Leased Lines Directive* (92/44/EEC) as amended by the *Full Competition Amending Directive* (97/51/EC) requirements are imposed on operators to provide Quality of Service (QoS) data on leased lines which NRAs must collect and publish. However, the cut-off point for this is at speeds of 2Mbit/s. Although this was reasonable in 1992, it is now too slow. The requirement must be extended to include 34, 45 and 155 Mbit/s leased lines.

INTUG Europe believes that the provision of such comparative data is essential for users. We believe that it is important to have comparative QoS data available both for individual member states and that it must be comparable across the internal market.