

Regulation of Wholesale-Only Operators under Article 80 of EECC

1. Introduction

The European Electronic Communications Code (EECC) sets out principles that define a wholesale-only operator in the EU and the regulatory measures to which a wholesale-only operator with significant market power (SMP) would and would not be susceptible. The concept of a wholesale-only operator is introduced in the EECC but was not in the original 2002 directives nor their 2009 update.

Under Article 80, where an NRA finds a Wholesale-only undertaking has SMP it:

“... may impose on that undertaking only obligations pursuant to Articles 70 [non-discrimination] and 73 [access to specific network elements on reasonable request] or relative to fair and reasonable pricing if justified on the basis of a market analysis including a prospective assessment of the likely behaviour of the undertaking designated as having significant market power.”¹

The NRA does not, other than in exceptional circumstances, have access to the remedies under Articles 69 (Transparency), 71 (Accounting Separation), 72 (access to Civil Engineering) or 74 (Price Control and Cost Accounting).

2. Definition of wholesale-only operator is restricted

2.1. Definition

A wholesale-only operator must meet two criteria, which are in summary:

1. It only has activities, current and planned for the future, in wholesale markets for electronic communications services and therefore does not have activities in any retail market for electronic communications services provided to end-users ²; and

¹ Article 80(3) of EECC

² Article 80(1a) of EECC

2. It is not bound to deal with a single and separate undertaking operating downstream that is active in any retail market for electronic communications services provided to end-users, because of an exclusive agreement, or an agreement which de facto amounts to an exclusive agreement.³

In interpreting the above definition of wholesale-only, the code includes any operator that “*is active in a wholesale market and also supplies retail services solely to business users larger than small and medium-sized enterprises.*”⁴

2.2. Many apparent wholesale operators are excluded

This strict definition would thus exclude undertakings where there is a minority shareholding in a wholesale operator, but the control of the operator rests with an owner who also provides retail services to small and medium-sized enterprises and/or residential end-users, whether in the same territory or elsewhere in the EU⁵.

For example, although Axione in France does not provide services directly to end-users, it is a subsidiary of (being 51% owned, and controlled by) Bouygues Group, which also owns 90.5% of the retail operator Bouygues Telecom, and thus its NRA would not be restricted by Article 80 if Axione were ever found to have SMP in a local region where it has network assets.

It is notable that the exclusion includes retail operations (except for sales to large enterprises) anywhere in the EU. Infrastructure investors such as Macquarie and PPK Group that own controlling stakes in telcos across several member states would need to divest retail activities in all states if they were to be eligible for Article 80 in instances where their local wholesale operators are found to have SMP.

2.3. Smaller wholesale operators may be found to have SMP in local markets

Today, there are a few smaller operators that would satisfy the definition of Wholesale-only under Article 80, but they do not currently have SMP in any market and thus would not in any case be susceptible to the relevant remedies by NRAS. Examples are Open Fiber (Italy), Gagnaveita Reykjavíkur (Iceland) and SIRO (Ireland). In the case of SIRO, Vodafone is a major investor, but SIRO is a joint venture with the electricity distributor ESB. Vodafone thus does

³ Article 80(1b) of EECC

⁴ Paragraph 208 of EECC recital

⁵ Article 80(1a) of EECC

not have control of the entity and in this case the NRA would be restricted by Article 80 were SIRO found to have SMP in any market.

As the EC notes in its recent draft guidance on market definitions⁶, it is likely that after the withdrawal of copper, NRAs will define sub-national markets for broadband; in these cases, smaller operators such as those above, who do not have a national network footprint may be found to have SMP if they are the only or main provider of FTTP in a local area.

2.4. Incumbents may demerge to create wholesale-only operators

However, the most likely immediate application of Article 80 will be where incumbent operators restructure. In Denmark and in Czechia, for example, the incumbent operators have recently voluntarily functionally separated into wholesale and retail operations (TDC NET/Nuuday and CETIN/O2 respectively) perhaps with the possibility of full separation at a later date.

2.5. Italian AccessCo – the likely first operator under Article 80

In Italy the process of demerger is further advanced. The incumbent TIM intends to transfer its fibre network to a subsidiary in which it owns 58%, and this company will subsequently merge with Open Fiber to create a larger wholesale operation. The deal will leave TIM with a majority ownership of the shares, but not, under the shareholder agreement, with control of the new undertaking and therefore Article 80 may apply. This demerger is intended to be completed by the end of Q1 2021.⁷

2.6. International examples

Although there are no examples of wholesale-only operators with SMP in the EU today, there are examples overseas. One example is Chorus in New Zealand, which was the result of a demerger of the former vertically integrated Telecom New Zealand (TNZ) in 2011. Although the NRA did not directly require TNZ to separate, the New Zealand government did not allow vertically integrated operators to bid for state funding of fibre networks and Chorus was thus created to be able to receive such funding. Another example is NetLinkTrust in Singapore, where the NRA has required the creation of a separate national operator of dark fibre.

⁶ Draft explanatory note accompanying draft commission recommendation on relevant product and service markets within the electronics communications sector susceptible to ex ante regulation..., section 2.5, pages 14 to 15

⁷ <https://www.lightreading.com/opticalip/fttx/tim-kkr-and-fastweb-agree-to-create-fiberkop/d/d-id/763570?>

2.7. Will Article 80 encourage further changes to operators' business models?

A factor that would influence an SMP operator's decision to demerge and form a wholesale-only operator would be whether or not it expects the sum of the value of each demerged entity to be greater than the value of the vertically integrated entity. That is, the valuation exercise would take into consideration the difference in the regulatory measures that might be imposed on a wholesale-only operator compared with the vertically integrated operator. In particular, a wholesale-only operator potentially avoids intrusive forms of regulated wholesale access prices for certain access services.

3. BCRD may allow NRAs to impose cost orientated controls on wholesale-only operators

Although, except in exceptional circumstances, Article 80 does not allow the NRA to apply article 72 (access to civil engineering) in the event of an SMP finding, the NRA may still be able to impose remedies under the Broadband Cost Reduction Directive (BCRD). As the EC notes in its draft explanatory note to its products and service market definition recommendation:

*... the BCRD mandates that **any network** ... meet all reasonable requests for access to its physical infrastructure under fair terms and conditions, including price. ... Access through the BCRD represents a dispute-resolution based intervention, and is not based on an ex ante intervention by the regulatory authority. [In Bulgaria], the provisions of national law implementing the BCRD, accompanied by extensive use by alternative operators of their own ducts, have been considered by the NRA as sufficient to ensure access to ducts and poles and hence the SMP access to PIA was lifted.⁸*

In Romania too, although no operator has been found to have SMP for broadband active services, price caps have been imposed under BCRD legislation if an operator is receiving public funds or other assistance – e.g. NetCity, which offers physical infrastructure and dark fibre access within the city of Bucharest. NetCity is today (and since 2017) a subsidiary of E-INFRA, a privately-owned group that also includes various non-telecom infrastructure operators in Romania, but which has no retail telecoms operations.

⁸ Draft explanatory note accompanying draft commission recommendation on relevant product and service markets within the electronics communications sector susceptible to ex ante regulation..., section 4.1, pages 55 to 56

NetCity is subject to a (fully allocated) cost-based price cap by the NRA, ANCOM, but this is not under the SMP regulations, but rather under local legislation (Law 159/2016) that implements the BCRD.

4. Article 80 allows NRAs to impose full remedies in certain situations

NRAs can impose additional remedies if they can show there is need to prevent adverse impact on competition. Paragraph 4 of Article 80 provides that :

"The national regulatory authority shall also review obligations imposed on the undertaking in accordance with this Article if on the basis of evidence of terms and conditions offered by the undertaking to its downstream customers, the authority concludes that competition problems have arisen or are likely to arise to the detriment of end-users which require the imposition of one or more obligations provided in Article 69, 71, 72 or 74, or the amendment of the obligations imposed in accordance with paragraph 2 of this Article."

This paragraph could be interpreted in different ways and may in practice give NRAs considerable discretion to apply any of the full range of SMP remedies to a wholesale-only operator. Indeed, the economic arguments that would explain why an operator should be exempt from these remedies, simply by virtue of being wholesale-only, are not clear.

5. If fair and reasonable pricing (and/or non-discrimination) is used as the SMP remedy under Article 80, what will that mean?

The expression "fair and reasonable" has not been widely used in telecoms regulations in Europe, although it is used in other legal contexts. Although it was introduced in the BCRD⁹, which as noted above has been used to impose price controls by NRAs, it has not generally been used for price restraints under SMP regulation.

One notable exception is Ofcom, which has used this concept widely as an alternative to imposing direct price controls or a more general requirement that prices be cost orientated.

Ofcom has explained the concept on three ways:

⁹ BCRD (Directive 2014/61/EU) Article 3, paragraphs 3 and 5

1. That prices should be consistent with a benchmark which is cost orientated (for example that the wholesale access prices for higher bandwidth local access services of KCOM (an operator with SMP in a local region) should be consistent with those of BT).¹⁰
2. That wholesale prices should not cause margin squeeze with retail prices of an SMP operator (i.e. the economic replicability test) e.g. wholesale line rental.¹¹
3. That wholesale prices should provide “*a reasonable return over costs including a reasonable contribution to common cost recovery*”¹²

However, as there have never been any formal disputes raised in respect of fair and reasonable pricing in the UK, more precise guidance has not been issued.

In France, in certain cases where it does not impose cost ordination requirements for prices, Arcep has instead imposed a requirement that the SMP operator should not impose excessive or predatory prices. In its current consultation on wholesale fixed markets it proposes the requirement of non-excessive pricing for certain legacy ATM services and for high-bandwidth fibre services in certain geographic areas and non-predatory pricing for high bandwidth services based upon FTTH technology¹³. Although the expression fair and reasonable is not used by ARCEP, these requirements appear analogous to those used by Ofcom in that context and so may indicate how Arcep will interpret this requirement in future.

Article 80(2) also states that an NRA may impose the non-discrimination obligations specified under Article 70. The 2013 Recommendation on consistent non-discrimination obligations may provide guidance on the application of this obligation, but the EC is presently consulting on updating the 2013 Recommendation, which raises uncertainty regarding the status of any relevant measures. One point that we suggest should be addressed in the updated recommendation is the application of the non-discrimination obligation, particularly the margin squeeze test for wholesale-only operators. The 2013 Recommendation addresses non-discrimination obligations and the margin squeeze test for SMP operators that vertically

¹⁰ Ofcom Hull Area Wholesale Fixed Telecoms Market Review 2021-26 Volume 3: Remedies, Consultation 16 July 2020, paragraph 2.19

¹¹ Ofcom Narrowband Market Review Statement 30 November 2017, paragraph 8.39

¹² Ofcom Hull Area Wholesale Fixed Telecoms Market Review 2021-26 Volume 3: Remedies, Consultation 16 July 2020, paragraph 2.16

¹³ Arcep, Consultation Publique du 7 juillet au 14 septembre 2020 Analyse du marché 4 de fourniture en gros d'accès de haute qualité : marché pertinent du haut et du très haut débit fixe / Projet de décision, Articles 30 to 32, page 104

integrate wholesale and retail services, but it does not explicitly address wholesale-only operators.

GOS is developing a separate paper on the non-discrimination obligations, specifically the application of the economic replicability test within this new context.

6. Conclusion

The restrictions on the actions of an NRA on wholesale-only operators is a new concept in EU telecoms regulation introduced by the EECC. Its practical implications are not fully clear as:

- There are currently no SMP operators that would qualify under Article 80, although the new Italian AccessCo expected to be created in 2021 is likely to do so
- NRAs may still be able to impose price and other restrictions under the BCRD
- Article 80 does allow extra remedies where there are competition concerns.
- The exact meaning of fair and reasonable pricing restrictions is not well developed, although France and the UK provide some limited precedents.

These matters will need to be clarified in the new EC guidance on NGA and the BEREC guidance on the EECC.

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