

**Response of COLT Telecom Group to the public Consultation  
of the European Commission on Community Guidelines for the application  
of State Aid rules in relation to rapid deployment of broadband networks**

## **1 Synthesis**

COLT Telecom Group SA [COLT] is a Pan-European Information & Communication Technology (ICT) service provider which has been building, developing and operating its fibre network infrastructure (incl. metropolitan fibre access in 32 European cities) and data centres addressing businesses throughout Europe since 1993. COLT has invested over € 4.5 Bn of its shareholders' money, is still re-investing 95% of its EBITDA, and has never paid a dividend. The majority (70%) shareholder of COLT still is its founder, Fidelity.

COLT thanks the Commission for submitting the draft guidelines to public consultation.

On the whole, we find that the Commission has tried to put out a balanced proposal and COLT has only limited improvements to propose. However if these suggestions were not followed, there is a clear risk for the Commission to give a negative signal to private investment.

Since COLT is a child of competition and is built for the long run, COLT does not fear competition, as long as competitors operate under the same rules as COLT.

Any competitor owing a return to a private shareholder plays under the same rules as COLT. On the contrary, COLT has a lot to fear from investments funded by the taxpayer and spent where COLT has already built a network.

COLT would like to emphasise the need to adopt the following principles: no State Aid or SGEI in black areas; any State Aid or SGEI must be subject to a requirement for open tender, and a requirement to provide open access, and associated terms and conditions that lead to preference for fibre P2P architecture.

## **2 Global comments**

### ***2.1 Treatment of State Aid for NGA networks when put forward as a Service of General Economic Interest (SGEI)***

Section 2 (The Commission Policy on State Aid for Broadband Projects) of the draft Guidelines carefully makes the distinction between projects submitted under Article 87(1) of the EC Treaty (Aid granted by Member States to undertakings) and under Article 86(2) (Services of General Economic Interest or SGEI). However section 3 (State Aid for NGA networks) does not make any specific reference to projects submitted under Article 86(2). The possibility for the Commission to question a Member State on the definition of a SGEI in the event of a manifest error, which is mentioned in section 2, should also be explicitly included in section 3.

## **2.2 State Aid in Broadband and NGA Networks: example of measures that grant resources to SGEIs free of charge, to the detriment of competitors**

Local Authorities in some Member-States tend to consider that, when they want to act for the digital development of their territory, and set up broadband or NGA SGEI for that reason, then other electronic communications operators should work for them free of charge. For instance, in France, article L.33-7 of the General Code of Posts & Electronic Communications, introduced through the Law for Modernising the Economy published on August 5, 2008 in the Official Journal of the French Republic, states that<sup>1</sup> : *“Undertakings managing electronic communications networks and electronic communications operators communicate the information related to the layout and deployment of their infrastructure and networks with no charge to the State, to the local authorities and to the groupings of local authorities, on their territory, upon their request”*.

This measure, implemented in a Decree dated February 12, 2009<sup>2</sup>, allows French local authorities to request communication of data, studies and information from telecoms operators free of charge, and to forward the same to competing telecoms operators<sup>3</sup>. In other words, French local authorities allow some operators to obtain, free of charge, information from their competitors that they should pay for under normal market conditions.

This is a clear case when SGEIs freely benefit from what other operators have to pay for, e.g. the studies of cable deployment in the ducts of France Telecom. Operators with infrastructure are also penalised by having to give away their network plans, in a format which they do not even have for their own use, to a local authority for the purpose of fostering a competitor to the existing electronic communications operators. The quantity of work implied by this measure is potentially enormous, if all local authorities with telecom projects ask for detailed maps and plans of networks to be delivered to them in a pre-defined vector format. Doing it would be huge effort and having to do it for free is a severe distortion of competition.

This is a clear example when the law of a Member State organises State Aid for the benefit of SGEIs in the field of broadband and NGA networks. The Guidelines should state clearly that asking competitors to do work for free for the benefit of one competitor is clearly State Aid and should be explicitly forbidden. A fair compensation of the operator delivering the work should be the rule.

### **3 Comments on the Introduction: the memory of the private investor**

Paragraph (5) of the draft Guidelines states that: *“The primary objective of State aid control in the field of broadband is therefore to ensure that State aid measures will result in a higher level of broadband coverage and penetration, or in a more timely manner, than would occur without the aid, and to ensure that the positive effects of aid outweigh its negative effects in terms of distortion of competition.”* Without coming back to 19<sup>th</sup> century investments in railways, and taking into account temporary irrational exuberance and economic bubbles,

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<sup>1</sup> CPCE Art. L. 33-7. – « Les gestionnaires d’infrastructures de communications électroniques et les opérateurs de communications électroniques communiquent gratuitement à l’Etat, aux collectivités territoriales et à leurs groupements, à leur demande, les informations relatives à l’implantation et au déploiement de leurs infrastructures et de leurs réseaux sur leur territoire. »

<sup>2</sup> Décret n° 2009-167 of 12 February 2009, JORF (French official journal), 14 February 2009

<sup>3</sup> See for instance Art. IV, 5th paragraph of the above-mentioned decree.

everyone accepts that private investors have a memory, and that any change in the rules governing private investments and their possible crowding out by subsequent public investment have a lasting effect on the private investor. Private investors accept more easily the ups and down of the economic cycle, or the investment by other private actors, because they have a certain degree of predictability, than the rotation of the regulatory “wheel of fortune”, because regulatory changes can alter the validity of private investment *a posteriori* and in unpredictable ways. In ensuring that “*the positive effects of aid outweigh its negative effects in terms of distortion of competition*”, the Commission should be aware of this long term impact on private infrastructure investor confidence of:

- changes in State Aid regulation for broadband
- or of changes in definitions of SGEIs
- or in a surge of (possibly duplicative) public investment as a substitute for private investment during an economic downturn.

## **4 Comments on Section 2 - Commission Policy on State Aid for Broadband Projects**

### ***4.1 Existing vs. new investment***

In paragraph 45, the draft Guidelines offer some degree of consideration for existing investment. However the mere prospect that a lot of public investment is there, waiting for a green light to be spent, is a clear signal that private investment in new areas is more risky than ever. If this private investment is about converting resale offers, wholesale broadband access, or copper unbundling to fibre-based solutions, there is still an incentive to improve an existing network to give it a new lease of life. But if this investment is about conquering new customers on new ground, then the private investor will drop any investment plan if he learns that the construction of a public network is being considered; in such a case, there is a clear risk that the prospect of public investment is enough to deter private investment. Similarly, if a fibre investor such as COLT is overbuilt by a publicly financed competitor, and sees (the prospect of) roll-out in areas to which privately funded expansion makes sense, the deterrence of private investment will be very clear.

### ***4.2 Setting the boundary between private and public investment by the nature of the expenditure***

One way to give a clear signal is to precisely say which components of a network can be built under public investment. If public investment was strictly limited to ducts and associated facilities, provided under non-discriminatory cost-oriented conditions, with fibre cables and electronics clearly left to private initiative, then the rules would be clear.

### ***4.3 Comments on section 2.2.2 - Public service compensation and the Altmark criteria***

COLT has always argued that the Altmark criteria are inadequate in the case of intensive public investment hampering the profitability of intensive private investments. Even if, under French law (article L.1425-1 of the General Code of Local Authorities), an SGEI on electronic communications infrastructure is not legally bound to providing evidence of a market failure before it can be defined/adopted, the economic justification of an SGEI is a market failure. Such a market failure can be defined only vis-à-vis a given requirement (in

terms of nature of the service, of price or of area covered). Economic theory tells thus that market failures are due to price inefficiencies caused by behavioural bias. In other words, the private service is too expensive because there is not enough competition. As a consequence, this private service is not sufficiently consumed. Hence an alternative subsidised public service must be put at the disposal of the public, in order to push the use of the service to the optimum level decided by the political authority. The capital-intensive variant of this theory is that the service is not sufficiently consumed because the spontaneous deployment of private infrastructure is not fast enough. Hence the political authority must invest in order to accelerate deployment and reduce prices. As a consequence, the damage incurred by a partial<sup>4</sup> competitor to the public service could be analysed by the advocates of the public service as an illegitimate profit, because this private competitor would be unduly exploiting a situation of under-investment in order to maintain too high prices.

The partial competitor to the public service could reply: “My profit is not excessive. As a proof of it, I am still incurring losses, or I would be if prudential rules (IAS16) had not forced me to write off my assets for prudential reasons”.

The defender of the public service could answer two things:

- Either your investment brings too low a return because you have not invested enough. If you had covered 100% of the territory your returns would have been increasing and not diminishing. This is the logic of the private investor principle, as illustrated by the Amsterdam CityNet case.
- Or 100% of this territory must be covered and this deserves a subsidy. However I can minimise the subsidy by allowing my private contractor to cover part of his deficit in unprofitable areas by skimming profitable areas. This is the case defended by the Hauts-de-Seine project in France.

The central question which the Altmark criteria applied to SGEIs does not answer is not the market failure per se (too high a price or too small a deployment) but the right of the public authority to finance the compensation of the market failure by the pre-emption of the profitable part of the market. In other terms, even when putting aside the relevance of the optimal use of a service by the political authority, two questions can be deduced:

- Should the price paid by those who are ready to pay more than the price of the public service be the price of the public service (based on non-discrimination) or the price they would pay if there was no public service?
- Can revenues covering the fixed costs incurred by the private providers of services answering solvable demand in the absence of a public service be captured thanks to the public financing granted to provide the public service?

A parallel analysis of the universal service (hereafter US) for fixed telephony in France on the one hand and of the public service for fibre optics in the Hauts-de-Seine (the so-called THD92 project) illustrates the importance of these two questions:

- US consists in setting a “reasonable” price for the service but this price is now the highest on the market (actually it has become a Ramsey pricing); there are social tariffs for those who cannot afford to pay this price; France Telecom, the universal service operator, is compensated on an annual basis for the net cost of being the provider of the universal service, according to its losses in unprofitable areas duly

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<sup>4</sup> A partial competitor is a competitor who does not pretend to offer everything that the public service is offering or who offers it on a limited scale or at a higher price.

defined under the control of ARCEP, the French NRA; accordingly, there is no possibility for the provider of the universal service to capture business in profitable areas by the mere fact of providing the service in unprofitable areas;

- THD92 also sets a price which is labelled as “reasonable”; this price, however, is the lowest on the market; there are no social tariffs; the provider of this public service would, if authorised by the Commission, be compensated once and for all as having proposed the lowest price in a competitive call for tenders, by a subsidy to build a network, paid for no matter whether the network is built in profitable or in non-profitable areas; there is a clear possibility to capture business in profitable areas by providing an activity in a non-profitable area.

How could the Altmark criteria be perfected in order to prevent such a pre-emption, when the universality of a public service is used as a leverage to reduce its cost, at the expense of the actors serving the part of the market which does not need a public service? Questioning the SGEI in this case is not questioning the political definition of the market failure (this could be done in other arenas, but is not what the Commission is supposed to do) but questioning the excessive nature of the remedy.

What COLT is asking for is that the method used to calculate compensation to a SGEI consists in clearly earmarking the areas for which the provision of the SGEI is unprofitable for private investors, publishing the maps of these areas and restricting the payment of the subsidy to actual deployment in the unprofitable areas. This does not imply that the SGEI is provided in the unprofitable areas only, but that the compensation is.

#### **4.4 SGEIs and business telecoms: which overlap?**

In paragraph 23, the draft Guidelines state that: “*the Commission has ruled that the notion of a SGEI and the subsequent reliance on the Altmark case-law could not be accepted where the provider had neither a clear mandate nor was he under any obligation to provide broadband access to and connect all citizens and businesses in underserved areas but was more oriented towards connecting business*”. COLT is asking for the following: in a region where a private investor has built a fibre network to serve businesses but no operator has built a fibre network to serve residential customers, strict safeguards should be put in place in order to avoid that, should a SGEI be built in this area, it would not be allowed to serve businesses on conditions distorted by measures designed to help it to address the residential market.

#### **4.5 Under-served areas: which granularity?**

Paragraph 23 also raises the following question: what is the level of granularity with which underserved areas can be defined? Sub-national market analyses suggest that the granularity can go from the region to the building. The fractal nature of an under-served area makes this level of granularity a very difficult choice.

COLT thinks that an under-served area should be defined at the level of the building. Any higher granularity encompasses the risk of pre-emption of the served areas by the SGEI.

## **4.6 Claw-back mechanisms**

In paragraph 45 h, the claw-back mechanism to avoid over-compensation (a reimbursement of the subsidy) should be considered with much caution. More generally, claw-back mechanisms of all kinds (more often for the profit of the contractor than of the public authority) are often nested in contracts granted to private companies to run a public service. When profit is capped, often so are losses. Such losses may result either from lower demand than expected, or from a change in regulatory conditions. This is where private companies running a public service often enjoy a free lunch: if the NRA decided to cut the price of their wholesale services, then they would trigger the claw-back clause and have the public authority foot the bill. This is a clear case of bad governance with private profits guaranteed for one actor by public losses. For instance, if a NRA was settling a dispute between an operator buying a wholesale offer and the SGEI providing this wholesale offer by cutting the price of the wholesale offer, then the SGEI provider would ask the local authority to foot the bill. As a consequence, the Guidelines should clearly state that no claw-back clause should be possible for a SGEI operator to claim for losses of any kind.

## **5 Comments on Section 3 - State Aid for NGA Networks**

### **5.1 P2P FTTH should be part of the definition of NGA**

Paragraph 48 of the draft Guidelines is defining Next Generation Access as:

- (i) *laying fibre to existing street cabinets offering the prospects of downstream bandwidths of a minimum of 40 Mbps and 15 Mbps upstream (compared with today's downstream speeds of a maximum of 8 and 24 Mbps for ADSL and ADSL2+ access technologies, respectively);*
- (ii) *upgrading current cable networks to deliver speeds up to and beyond 50 Mbps against the previous maximum speed of 20 Mbps, using the new 'DOCSIS 3.0' cable modem standard, or*
- (iii) *connecting newly built homes and offices with fibre connections offering services up to 100 Mbps and beyond.*

The surprising point in this definition is the restriction of *fibre connections offering services up to 100 Mbps and beyond to newly built homes and offices*. Deploying the same connections in existing buildings should qualify as NGA as much as if the buildings were newly built.

### **5.2 A five year window of opportunity for private NGAs might freeze a lot of private investment**

The 5 year reprieve put forward in paragraphs 65 and 73 to areas where private investors have are deploying or planning to deploy a Next Generation Access network, before considering that the area is not “NGA-black”, is placing private shareholders and managers of existing networks in front of a tough challenge:

- Either they invest fresh money provided by shareholders, independently from the profitability of existing operations, but they must be rather sure to improve their margins on their existing business, in which case their 5-year investment target can be reasonably predictable;
- Or they only invest the cash flow generated by their EBITDA after repayment of their debt, and then this 5-year capex target is a volatile amount on which they cannot formally commit to building NGAs in a given area. In this case the conversion of their existing network into an NGA in 5 years is beyond what they can commit to.

The capex flow of the last 5 years as mentioned in paragraph 73 may not be the right way to predict the capex flow of the next five years.

COLT is suggesting that the burden of the intention to get an area served within 5 years should be put on the public investor, with an obligation to inform private investors in the area beforehand, at the beginning of the 5-year reprieve period. However, the area where an SGEI NGA network could be subsidised would be limited by the areas not covered by the private networks at the end of the 5-year period.

### ***5.3 Wholesale access obligations for business services should be made permanent***

In paragraph 74 the 7-year obligation of wholesale access is not making this facility very palatable for those who would be in a position to ask for such access. First of all, the characteristics of the wholesale access to be provided are very unclear, and secondly it would mean that, unless they quickly climb the rungs of the ladder of investment all the way to building their own infrastructure, the rungs could disappear from under their feet. Regarding residential players which are viable only with a respectable market share (e.g. over 15%), this might be acceptable in some specific areas. However a business-only infrastructure player such as COLT needs permanent fit-for-purpose wholesale access in the form of high QoS layer 2 bitstream giving the access taker the ability to define its own services in order to serve business customers outside of its respectable but limited on-net area. For COLT, off-net is not a business per se, but a way to complement contracts which are mainly for on-net connectivity, and which would be lost if off-net could not be addressed. COLT is therefore requesting that, wherever a SGEI NGA network is built, wholesale business-grade wholesale access is made available not for 7 years but on a permanent basis.

### ***5.4 Setting the boundary between private and public investment by the nature of the expenditure***

As stated in section 4.2 above, a way to give a clear signal to private and public NGA builders is to precisely say which components of a network can be built under public investment. If public investment was strictly limited to ducts and associated facilities, provided under non-discriminatory cost-oriented conditions, with fibre cables and electronics clearly left to private initiative, then the rules for NGA aid would be clear.

## **6 Interaction between the draft Guidelines and the proposed Recommendation on Regulated Access to NGAs**

The second public consultation of the European Commission on its draft Recommendation on regulated access to Next Generation Access networks runs until July 24, 2009. It is not the purpose of this COLT contribution to provide a full response to this draft. However Appendix 3 to this draft recommendation looks extremely dangerous in terms of facilitating potential cartel behaviour and of pre-emption of objective market analysis. There is a sharp contrast between the draft guidelines on State Aid, which leave the Commission free to take a position on a given case and the draft Recommendation on NGA, which seeks to decide things beforehand. The pre-defined solutions brought by the draft Recommendation on regulated

access to Next Generation Access networks cast a very serious doubt on the apparent balance of the draft guidelines on State aid.

## **7 Suggested Modifications to the draft Guidelines**

*(Add at the end of paragraph 5) In this respect, the mere prospect of early broadband deployment projects potentially taking place might be enough to deter private investors from deploying broadband.*

*(Add at the end of paragraph 45b) Although the SGEI can be defined as being provided in a whole territory, including both profitable and unprofitable areas, the open tender process will clearly earmark the areas for which the provision of the SGEI is unprofitable, publish the maps of these areas and restrict the payment of the subsidy to actual deployment in the unprofitable areas. The amount of the subsidy cannot exceed the amount of the expected marginal deficit in the unprofitable areas only.*

*(Add as paragraph 45e bis) Duct-only intervention. In grey areas, the main reason for only one provider to be present is often the (total or partial) absence of available ducts to lay down a fibre optic cable and of a building to install a new central office and turn long copper lines into short ones. By providing these civil works in grey areas, while several private investors enjoy relatively comparable market shares in black areas, a public investor can often trigger private broadband deployment by several players at a time.*

*(Replace paragraph 45h by the following one). Claw-back mechanisms should be avoided. Claw-back mechanisms, although introduced to avoid over-compensation, often are accompanied with symmetric measures to secure the provider of the SGEI against losses. Such protections against losses are actually triggered much more often than the repayment of aid in case of unexpectedly high success. As a consequence, no clause should change the amount of a subsidy ex post, neither if demand for broadband in the target area grows beyond anticipated levels, nor if demand does not reach such levels, nor if changes in regulation modify the economic conditions under which the service is provided.*

*2.4 Free of charge provision of services by electronic communications operators to an SGEI through intervention of State or local Authorities should be considered as State Aid to the SGEI*

*(45 bis) Any State or local Authority requesting work to be done by an electronic communications operator (e.g. providing detailed network maps) should provide a fair compensation for this work. Any SGEI operator receiving the result of this work should pay its full price.*

*(48) For the purpose of the present Guidelines and without prejudice to any market definition carried out under the rules of the regulatory framework for electronic communications, in applying the State aid rules a NGA network is further defined as involving: (i) laying fibre to existing street cabinets offering the prospects of downstream bandwidths of a minimum of 40 Mbps and 15 Mbps upstream (compared with today's downstream speeds of a maximum of 8 and 24 Mbps for*

ADSL and ADSL2+ access technologies, respectively); (ii) upgrading current cable networks to deliver speeds up to and beyond 50 Mbps against the previous maximum speed of 20 Mbps, using the new 'DOCSIS 3.0' cable modem standard, or (iii) connecting ~~newly built~~ homes and offices with fibre connections offering services up to 100 Mbps and beyond.

(54 bis) “In some instances Member States may consider that the provision of a Next Generation Access network and services should be regarded as a public service or a service of a general economic interest within the meaning of Article 86(2) of the Treaty. According to the jurisprudence, although Member States have wide discretion to define what they regard as services of general economic interest or a public service task, the definition of such services or tasks by a Member State can be questioned by the Commission in the event of a manifest error. In this respect, the Commission will consider that in areas where private investors have already invested in a broadband network infrastructure capable of delivering Next Generation Access (or are in the process of geographically expanding such network infrastructure) and are already providing competitive Next Generation broadband services with an adequate coverage and bandwidth, setting up a parallel competitive and publicly-funded Next Generation Access infrastructure could not be considered as a public service within the meaning of the Altmark case-law or as a SGEI within the meaning of Article 86 of the Treaty.”

(54 ter) In a region where a private investor has built a fibre network to serve businesses but no operator has built a fibre network to serve residential customers, strict safeguards should be put in place in order to avoid that, should a SGEI be built in this area, it could serve businesses on market conditions distorted by measures designed to help it to address the residential market.

(54 quater) Duct-only intervention. In grey areas, the main reason for only one provider to be present is often the (total or partial) absence of available ducts to lay down a fibre optic cable. By providing these civil works in grey areas, while several private investors enjoy relatively comparable market shares in black areas, a public investor can potentially trigger private NGA deployment by several players at a time.

(Add at the end of paragraph 65) In case a public investor disagrees with this classification, the burden of the intention to get an area served within 5 years should be put on the public investor, with an obligation to inform private investors in the area beforehand, at the beginning of the 5-year reprieve period. However, the area where an SGEI NGA network could be subsidised would be limited by the areas not covered by the private networks at the end of the 5-year period.

(Add as a new bullet point at the end of paragraph 74)

- The 7-year and 10-year periods mentioned in paragraph (74) for which wholesale access should be granted apply for residential-grade offers only. Business-grade wholesale access offers should be made permanent. This is to take into account the limited economies of scale enjoyed by business-only operators who need wholesale access offers as a permanent means to complement their on-net offers.