



Proposed EU State Aid Guidelines for Broadband Networks Deployment

Response of Vodafone Group

Private investment is more likely to achieve the Community's objectives

Whilst Vodafone recognises the importance of the expansion of broadband networks to economic growth in the EU, the investment required to roll-out in particular NGA networks in Europe is sizeable and investing financial resources on such a scale entails substantial business risks. Given the funding needs and the fiscal position of most Member States, the lion share of NGA funds will come from private investors who are prepared to take these risks. Only private investors are in a position to deploy the next generation of technologies and services that will deliver a competitive NGA market.

But private investment alone will not be sufficient to roll-out NGA networks to less densely populated areas and thereby increasing the digital divide even further. It therefore must be the objective of these Guidelines to create an environment which allows for private and public investment to co-exist and where public investment complements the privately funded roll-out areas.

But state intervention also needs to contribute to the lowering of investment costs via appropriate measures aimed at granting access to existing civil infrastructures and fostering the sharing of civil works. For example all ducts whether they are public (municipalities) or private (utilities, telecoms and cable operators) that can facilitate the NGA roll-out should be accessible for the deployment of new NGA infrastructure.

The need for alternative investment models for broadband expansion

Considering the impacts that public intervention can have on NGA investment, State Aid rules must be considered as part of the overall European broadband strategy and must therefore be in line with the EU Recommendations on regulated access to NGA networks.

Hence governments play a role in exploring and facilitating new and alternative possibilities for private investment that are better suited to overcome the challenges that the transition to NGA poses to the more traditional approaches to network investment. Simply rolling forward the current two models of competition – platform competition and the 'single firm – single network model – will not meet these challenges.

Unlike its first attempt to establish Recommendations for NGA Regulation the European Commission has recognized in the second draft Guidelines ¹ that the legacy approaches to network regulation were not sufficient to meet the described investment challenges .

There in Section 2 of Annex III, the Commission outlines a new co-operative approach that would allow multiple (more than 4) investors to finance, build and control a single fibre network infrastructure which will not be subject to SMP obligations as long as certain additional criteria are met. Such an alternative investment model would have a multitude of advantages over more traditional approaches to network competition. VF will comment separately in response to draft Recommendation

A co-investment approach² overcomes most of the challenges of the single network – single operator approach poses. In the single network – single firm model those who do not invest in network infrastructure require the intervention of the regulator to gain access. Co-investors however are vertically integrated operators that compete with each other in the downstream but also the wholesale market. A joint investment generates better network economies through, amongst other things, avoiding of asset duplication and improved access to capital which in turn will lead to improved NGA coverage. Where investors jointly finance NGA networks and provide NGA services this investment risk is significantly reduced.

The Guidelines create the risk of distortive premature state intervention

As the Commission itself recognises, state support for broadband deployment that fails to meet the market investor test will be likely to involve the provision of state aid that is incompatible with the operation of the common market. It is only if the criteria in Article 87(3)(a) and (c) are met that such aid could be approved by the Commission.

Currently aid measures that are designed to assist in regional development (and are in compliance with the Commission's Regional Aid Guidelines) or that promote an objective of common interest in a proportionate way may fall within the scope of Article 87(3)(a) or (c). To the extent that the conditions set out in the Regional Aid Guidelines are not met, Vodafone notes that the Commission has previously considered Article 87(3)(c) to be inapplicable to the provision of aid measures in regions where there are at least 2 existing infrastructure operators and the possibility exists (from a technical and commercial perspective) for these existing providers of broadband in a given region to upgrade or expand their existing network capabilities. In short, there must be evidence of market failure that the aid measure is designed to address.

The Commission has thus far been sceptical that in so-called 'black areas' where there are at least 2 infrastructure providers able to provide broadband services the benefits of state intervention

¹ 2nd Public Consultation on a revised draft Recommendation on regulated access to Next Generation Access networks, June 12th, 2009

² For clarity, Vodafone would like to point out that joint investment models that lead to a duopolistic market structure (as described in Section 1 of Annex III of the draft NGA Recommendation) should not be treated any different to an access monopoly.

outweigh the risk of crowding out future private investment.³ In these proposed Guidelines the Commission now proposes to adopt an alternative approach to aid measures in these 'black areas'. State funding for broadband network development in black areas may be deemed to be compatible with the common market where the Member State government is able to demonstrate that existing networks have failed to satisfy the demand of their customers or that there is no planned investment on the part of these existing networks over a forward looking period of 5 years.

Whilst Vodafone appreciates that there may be some circumstances in which these criteria may be met, the scope for private investment should be increased in light of the Commission's recently expressed support for certain models of co-investment. Such models are far more likely to promote competition than state intervention (for reasons set out above/below) whilst facilitating the growth of 'black areas',⁴ As the draft NGA Recommendation makes clear in Annex III Section 2, where specific conditions are met for joint deployment of FTTH networks the relevant market will be considered to be effectively competitive. Consequently, Vodafone would submit that for the purposes of state aid analysis that in areas where broadband networks are jointly deployed on the principles of the NGA Recommendation Member States should consider such areas to be 'black'. Put simply, it is not necessarily the number of existing networks that should be the threshold for determining the compatibility of any aid but the number of competitors committed to rolling out new broadband services, even if some of them all be dependent upon the same infrastructure.

Vodafone would strongly encourage Member State governments to be required by the Guidelines to also demonstrate that there is no prospect of co-investment before considering state intervention. Where co-investment exists or where there is a prospect for co-investment, a separate state funded network would be damaging as it would deter private investment. In the absence of an explicit requirement to examine the feasibility of co-investment, the Commission may inadvertently undermine the possible benefits of the NGA Recommendation. Member States may come to regard state aid as being *de rigueur* when in fact it should be seen to be unnecessary in areas where private investment should deliver innovation and growth.

The role of the state and the NGA Recommendation

Scope for state involvement in co-investment for network expansion

However, co-investment models do not preclude the involvement of the state in the expansion of broadband networks, where the state wishes to participate in such ventures on commercial terms. As the jurisprudence of the European courts has made clear, where the state acts on the basis on a private investor (the so-called 'market economy investor principle' or MEIP), there will be no presence of incompatible aid.⁵ Broadly, although the state as an actor pursuing economic policy aims may not be the same as a private investor seeking short-term profit where the state has acted in way that excludes the possibility of any profitability or return on investment in the long-term, incompatible aid is likely to be present.⁶ In the specific case of state support for broadband

³ Commission Decision C 35/2005 *Appingedam*, paragraphs 76-79 and footnote 30

⁴ As noted above, network access duopolies as envisaged by the draft NGA Recommendations in Section 1, Annex III can not automatically be deemed competitive and hence a 'black area'.

⁵ Case C-234/84 *Belgium v Commission*

⁶ Case C-305/89, *Italy v Commission*, paragraph 20; Case C-303/88, *Italy v Commission*, paragraph 22

network development and expansion, the Commission has applied the MEIP test in some detail when considering the support of the municipal authorities in Amsterdam for a public-private venture the development of a fibre-to-home network in Amsterdam. As that decision makes clear, the Commission will scrutinise carefully the extent to which investments by private undertakings occur at the same time, are of economic significance and are on the same terms as that of the state. As part of this analysis the viability of any business plan that has been drawn up and endorsed by both the state and private actors will need to be assessed.⁷ As this case makes clear, it is therefore possible for the state to become involved in broadband network expansion (including through models such as co-investment), but in a way that does not raise concerns under Article 87(1) of the EC Treaty.

Conditions for public funding of broadband networks

However where an analysis of all private investment alternatives will not lead to the deployment of a sufficiently large or sufficiently competitive network and where other public interventions (easing the acquisition of process of rights of way, mandated access to available duct infrastructure, etc.) state aid has an important role to play.

We support the Commission particularly in its efforts to relax the criteria for the application of Article 87(3)(c) where there are no other means of encouraging network investments and to make the approval of state aid conditional on measures that ensure competitive access.

We strongly endorse the Commission's view that measures should be put in place to limit the distortions of competition. Although we agree that these measures should include the obligation on the operator of subsidized network to provide wholesale access we believe that such an open access obligation can only be withdrawn when justified by the market conditions. We would also agree that subsidized networks should be capable of supporting of FTTH point to point multi-fibre architectures or an architecture that can be unbundled. These types of remedies or commitments are clearly necessary to ensure that the overall impact of the intervention of the state on competition will be positive. On the other hand, public resources should not be used to fund the development of network architectures that do not maximize the prospects of downstream competition such as FTTH GPON. . Such a differentiated treatment of certain forms of network architectures is appropriate when technology choices have such significant consequences for downstream competition.

Application of the Guidelines to the expansion and development of mobile broadband

Vodafone considers that the proposed principles governing state funded broadband network expansion should have a wider applicability than is currently proposed by the Guidelines. As the Commission will be aware, new innovative high speed broadband services may be provided across

⁷ Commission Decision C 53/2006, *Amsterdam*, paragraphs 91-95

mobile as well as fixed infrastructures, and in particular over the next generation of mobile networks (LTE). This next generation of mobile networks is likely to play an equally important role in expanding the geographic scope of broadband services. Co-investment models or network sharing initiatives may be similarly effective in facilitating the expansion of these mobile networks, whilst preserving fiercely competitive retail markets. However, there may be circumstances, as in the case of fixed networks, where private investment may be insufficient to deliver the upgrade to and expansion of existing mobile networks. Vodafone therefore encourages the Commission to broaden the scope of the proposed state aid guidelines to enable state funding for the deployment of the next generation of mobile networks in areas where there is little or no prospect of private initiatives producing this network expansion. Such guidance or clarification would be particularly welcome to both private market actors and EU Member State governments at a time when a range of different initiatives to facilitate the expansion of mobile broadband services are under active consideration.⁸

⁸ See for example *Digital Britain – The Final Report* (16 June 2009) at http://www.culture.gov.uk/what_we_do/broadcasting/6216.aspx