



EUROPEAN COMMISSION

Brussels, 02.VII.2008

C(2008)3176 final

PUBLIC VERSION

WORKING LANGUAGE

**This document is made available for
information purposes only.**

Subject: **N 250/2008 - Italy**
 Broadband connections for Alto Adige II

I. PROCEDURE

- (1) By letter registered on 20 May 2008, the Italian authorities notified to the Commission their project to support the development of Broadband connections for Alto Adige ("the notified measure" hereafter), pursuant to Article 88 (3) of the EC Treaty. Based on the information submitted, the Commission has completed its assessment of the project.

II. CONTEXT

- (2) The development of broadband connectivity in the territory of Alto Adige (autonomous province of Bolzano) is uneven. The territory is typically alpine: 85.9% is above 1 000 metres. One third of the 483 000 inhabitants live in the three main towns, Bolzano, Merano and Bressanone. Although around 80% of the population of Alto Adige has access to ADSL connections, the service is less available in mountainous areas where investment costs are higher than in densely populated areas, with service ratios as follows:

- 44 communes are below 50% (of which 40 have not any service);
- 31 communes are between 50 and 90%;
- 41 communes are above 90%.

- (3) Broadband connectivity¹ fosters the use of information and communication technologies and hence, the development of knowledge-based economies. Broadband connectivity accelerates the contribution of these technologies to economic growth, social development and innovation.
- (4) In order to offer widespread access to broadband technology in Alto Adige, the Provincial Council, in its deliberation N°646 of 7 March 2005, set out the objective to have broadband connections available for 90% of the population, 95% of enterprises with three workers or less and all enterprises with more than three workers by 2009. The attainment of those objectives in a number of communes was the object of the state aid measure approved by Commission decision of 10 October 2007 in case N-437/2007 – IT "Broadband Connections for Alto Adige". That measure, which is now being implemented, addressed the lack of broadband coverage at affordable prices for 44 communes in which such services are not available.
- (5) The notified measure covers broadband connections for additional communes which were not covered by the measure approved by the Commission. The financing of the notified measure results from a re-assignment of unspent funds from the 2008 budget of the province of Bolzano, which will be now used to secure additional coverage in the province. The measure approved by the Commission on 10 October 2007 and the newly notified measure are nearly identical in their design.

III. SUMMARY DESCRIPTION OF THE MEASURE

- (6) *Objective:* The notified measure supports primarily regional development objectives. The objectives are pursued through support to a procurement contract for the construction and operation of infrastructure to provide access to broadband services in determined communes of Alto Adige. Such services shall be supplied to business and residential customers.
- (7) *Legal basis:* The measure is based on the Legislative Decree of 1 August 2003 n.259: "Codice delle comunicazioni elettroniche", law L.P. 33/1982 "Provvedimenti in materia di informatica nella Provincia di Bolzano", the Deliberation n° 646 of 7 March 2005 of the Provincial Council: "Programma operativo per lo sviluppo della Società per l'Informazione in Alto Adige e-Südtirol 2004 - 2008 con particolare riferimento agli obiettivi per la messa a disposizione di una offerta di banda larga a copertura dell'Alto Adige".
- (8) *Procurement:* The measure will give rise to one tender to which operators licensed by the Italian Ministry of Communications can concur, individually or grouped. The contractor will build, own and operate the infrastructure.
- (9) *Target areas:* The project is aimed at 38 communes of Alto Adige, in which the infrastructure shall ensure fulfilment of the coverage objectives set out in the deliberation n°646 of the Provincial Council referred to above. In 13 of these, there is

¹ Broadband services can be delivered using various combinations of communications network technologies ("platforms"). Technologies can feature either fixed or radio based transmission infrastructure, and they can substitute or complement each other according to the individual situation. Current mass-market broadband services have generally download speeds starting from 512Kbit/s/ - 1Mbit/s. For business users, much higher speeds are needed.

no broadband service at all at present. As to the other 25 communes, the measure covers non-serviced fractions of their territory. None of the communes or areas in question is populated in excess of 1 500 households.

- (10) *Budget and funding instrument:* Up to EUR 7 000 000 will be paid to the selected operator from funds from the Autonomous Province of Bolzano.
- (11) *Beneficiaries:* The direct beneficiary of the measure will be the selected operator.
- (12) *Aid intensity:* The financial incentive intends to bring the break-even point of the investment made by the network operator within allegedly sustainable terms so that, in practice, the break-even is reached within 36 months from the supply of the service. The maximum aid intensity will depend on the offer presented by the successful bidder. The support covers no more than the estimated loss of the selected operator within the 36 month period.
- (13) *Duration of the measure:* The contract with the successful bidder will be signed for ten years. The support will be put into effect up to 31 December 2010 in three instalments: 80% on delivery of the services, and twice 10% following successful completion of service quality tests specified in the tender documents each of the subsequent years.
- (14) *Procurement:* The call for tender specifies the following requirements, among others:
 - *Technology and existing infrastructure:* no particular technology of the network is specified; the network can be built partly on existing infrastructure so as to avoid duplication.
 - *Wholesale supply:* the network operator shall grant non-discriminatory access to the network to all licensed operators or service providers allowing them to replicate all of its own retail offers.
 - *Tariffs:* the operator shall apply non-discriminatory, cost-based tariffs, which should be comparable to average tariffs in areas where the service is already provided. The tariffs must be proposed for the 10-year duration of the contract and shall not be revised without prior consent of the authorities.
 - *Award criteria:* the bids will be scored based on economic aspects such as tariffs and incentive support requested (max. 27 points) and technical factors such as quality and quantity of services proposed (max. 73 points).
 - *Monitoring and clawback mechanism:* The Italian authorities will monitor the execution of the business plan supplied in the tender within 36 months of successful completion and, in case receipts are higher or the costs lower than anticipated, the amount of the aid to reach break-even, plus applicable interest will have to be refunded in due proportion.
 - *Compliance with state aid rules and non recovered unlawful aid:* The contract is subject to a Commission decision of compatibility with State aid rules. The Italian authorities have also provided a commitment to suspend the payment of the aid to companies that have not reimbursed or put on a blocked bank account any aid,

including interests, which the Commission has decided to be unlawful or incompatible.

IV. ASSESSMENT OF THE MEASURE: PRESENCE OF AID

- (15) According to the EC Treaty and consolidated case-law, there is State aid within the meaning of Article 87(1) when:
- there is an intervention by the State or through State resources;
 - it confers an economic advantage on the recipient;
 - it distorts or threatens to distort competition;
 - the intervention is liable to affect trade between Member States.

State resources

- (16) The funds are disbursed by the Autonomous Province of Bolzano. State resources are thus involved.

Economic advantage

- (17) *Selected telecommunication operators:* The operator which shall be selected by open tender receives financial support which provides the possibility of establishing its business in the 38 communes of the Alto Adige targeted by the measure and, through coverage of losses incurred in the initial stages of the project, on conditions not otherwise available on the market. It is likely that the State intervention will allow the operator to offer the services at lower prices than if it had to bear all the costs itself and, as a consequence, such a service provider will be able to attract more customers than under normal market conditions.
- (18) *Third party providers:* In most of the areas covered by the project, there is no broadband connection and therefore no broadband wholesale offer at all. Therefore, third party providers of broadband services which do not have their own infrastructure and which use wholesale access provided under the measure might also benefit from the State resources, as they will be customers of the selected telecommunication operators.

Distortion of competition

- (19) The intervention of the State alters the existing market conditions by allowing the provision of broadband services by the selected telecommunication operator and, potentially, third party providers. A number of firms are likely to subscribe to the services provided by the selected suppliers to the detriment of more expensive market-based solutions (for instance satellite). Therefore, the fact that a new broadband service becomes available at a lower price than under market conditions has the effect of distorting competition.

- (20) In addition, while the Italian authorities decided to intervene precisely in view of the lack of private initiatives in at least some of the concerned areas, it cannot be excluded that market initiatives could become viable in some areas in the long term. The chosen operator will be capable of establishing its business and developing its customer base earlier than prospective competitors, enjoying a first mover advantage over them.
- (21) The scheme is also selective in that it is addressed to undertakings active only in certain regions and/or in the provision of broadband services, to the exclusion of other electronic communications services. These selectivity elements also induce a potential distortion of competition.

Effect on trade

- (22) Insofar as the intervention is liable to affect providers of electronic communications services from other Member States, the measure has an effect on trade. The markets for electronic communications services are open to competition between operators and service providers, which generally engage in activities that are subject to trade between Member States. There may also be an effect on trade between the businesses using the broadband services enabled by the measure and their competitors in other Member States.

Conclusion

- (23) In view of the above, the Commission considers that the notified measure grants an economic advantage to the selected operator, third party operators and undertakings that exercise an economic activity. The project is publicly funded, distorts competition and has an effect on trade between Member States. Therefore the Commission regards the notified measure as constituting State aid within the meaning of Article 87 (1) of the EC Treaty.
- (24) Having established that the project involves aid within the meaning of Article 87(1) of the EC Treaty, it is necessary to consider whether the measure can be found to be compatible with the common market.

V. ASSESSMENT OF THE MEASURE: COMPATIBILITY

- (25) The Commission notes that the project aims to ensure the widespread availability and use of high-speed broadband services in currently unconnected areas of Alto Adige with no prospect for coverage on commercial terms in the near and medium term and, as such, does not fall under one of the existing frameworks and guidelines.
- (26) The Commission therefore considers that the assessment of the compatibility of the measure with the common market needs to be based directly on Article 87(3)(c) of the EC Treaty² which states that:

² This approach was also followed by the Commission in other cases, see for instance: State aid decisions for the UK: N126/04 “Broadband for SMEs in Lincolnshire” of 14.12.2004, N199/04 “Broadband business fund” of 16.11.2004, N307/04 “Broadband in Scotland – remote and rural areas” of 16.11.2004 (See: http://europa.eu.int/comm/secretariat_general/sgb/state_aids/).

“aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest”

may be considered to be compatible with the common market.

- (27) In order to be compatible under article 87(3)(c), an aid must pursue an objective of common interest in a necessary and proportionate way. In this regard, the Commission considers it appropriate to assess the following questions:
- (1) Is the aid measure aimed at a well-defined objective of common interest (i.e. does the proposed aid address a market failure or other objective)?
 - (2) Is the aid well designed to deliver the objective of common interest? In particular:
 - (a) Is the aid measure an appropriate instrument?
 - (b) Is there an incentive effect, i.e. does the aid change the behaviour of firms?
 - (c) Is the aid measure proportional, i.e. could the same change in behaviour be obtained with less aid?
 - (3) Are the distortions of competition and the effect on trade limited, so that the overall balance is positive?

5.1. The support of broadband rollout is in line with the common interest

Community policy

- (28) Broadband services enhance the interpenetration between Member States and people which the treaty aims to bring about. As outlined in its Communication “i2010 – A European Information Society for growth and employment”³ and the eEurope Action Plan 2005⁴, the Commission actively supports the widespread availability of broadband services. There is evidence of regional development benefits resulting from greater broadband deployment, including job creation and retention as well as improved health and education services⁵. In order to achieve better broadband coverage, the Commission encourages Member States to put comprehensive national broadband strategies in place⁶. The measure at hand forms an important part of the broadband strategy in Alto Adige and complements, geography-wise, an aid measure already approved by the Commission. By improving broadband access for citizens and businesses in mountainous and sparsely populated areas of Alto Adige where these

³ COM(2005)229 final, 1 June 2005.

⁴ COM(2002)263 final, “eEurope 2005: An information society for all”.

⁵ For an overview, see: Lehr, Osorio, Gillet and Sirbu (2005): “Measuring Broadband’s Economic Impact”, and Orazem, Peter, University of Kansas Business School (2005), “The Impact of High-Speed Internet Access on Local Economic Growth”.

⁶ Commission Communication COM(2004) 369 of 12.05.2004, “Connecting Europe at High Speed – National Broadband Strategies”.

services are not yet available, the measure helps achieving greater cohesion and is therefore in line with the common interest.

Cohesion objective and market failure considerations

- (29) Lack of broadband coverage is due, among others, to some of the typical economic problems associated with networks industries. As the development of broadband connections in Alto Adige itself shows, due to economics of density, broadband networks are generally more profitable to roll-out where potential demand is higher and concentrated, in readily accessible areas which are more densely populated. Because of high fixed costs, unit costs escalate dramatically as population densities drop. Remoteness and relief also require bridging longer distances in the backhaul and in the last mile. In other cases it has been estimated that approximately 65-70% of the costs associated with the deployment of broadband in the access network is related to civil infrastructure⁷. In addition, although equipment costs fall as volumes increase, they remain a significant cost and major barrier to roll-out. In mountainous and sparsely populated areas of Alto Adige where demand is low and coverage of cost is uncertain or delayed, private operators have so far found it difficult to fund broadband infrastructure, which has a long life and amortisation period.
- (30) Hence, by providing financial support for the establishment of infrastructure to provide basic wholesale and retail broadband services in such areas of Alto Adige, the authorities pursue genuine cohesion and development objectives.

5.2. Well-designed aid

(a) Aid is the appropriate instrument

- (31) This intervention is part of several instruments that support the development of broadband connection in Italy, and more specifically in Alto Adige.
- (32) Tariff and access regulation imposed by the Italian regulator is one of those instruments. However, regulation was a necessary but not sufficient instrument to enable the supply of broadband in rural and remote regions as alternative providers need to combine the use of wholesale products from the incumbent with their own network investments which may not be profitable in areas where demand is low such as the target area of the Alto Adige.
- (33) In view of the limited availability –if at all- of broadband in rural and remote areas of Alto Adige, the Commission considers that the support provided by the notified measure is an appropriate instrument to achieve the set objectives.

⁷ Broadband Stakeholders Group “Broadband in Rural Areas”, 2003.

(b) The aid provides the right incentives to operators

- (34) The direct beneficiary of the aid will be selected by public tender in which bidders will submit a business plans indicating the amount of aid that they considered to be necessary to break even on the investment given the anticipated capital and operating costs and anticipated revenues. Prospective contractors are therefore encouraged to operate efficiently by minimising estimated losses with little room to inflate planned tariffs. Therefore, the aid should provide a direct and appropriate investment incentive for the selected operator.

(c) Proportionality

- (35) The Italian authorities have designed the measure in such a way as to diminish the possible amount of State aid involved and potential distortions of competition arising from the measure. In this respect, the Commission notes, inter alia, the following positive elements in the design of the measure:

- (a) *Open tender*: the recipient of the aid will be selected by open tender, awarded to the economically advantageous offer within the meaning of Article 55 of Directive 2004/17/CE.
- (b) *Wholesale access*: The selected operators will have to provide access to the subsidised networks to other operators on equal and non-discriminatory terms that will enable the latter to replicate their formers' offers.
- (c) *Effects on existing infrastructure providers and operators*: The freedom for the service providers to choose the most efficient way of procuring the necessary infrastructure, either by building, buying or leasing it from third parties minimises duplication, which may be liable to enhance economic efficiency. Existing operators have the possibility to contribute their infrastructure to the project, which limits its economic impact for operators that may already have infrastructure in place.
- (d) *Limitation of tariff discretion*: The selected operators will have to offer retail services at prices that are comparable to the average prices in areas where the service already exists, based on investment costs that can be deemed to be lower than the current investment costs at hand.
- (e) *Technological neutrality*: The project is technologically neutral, i.e. it does not favour a priori any given technology.
- (f) *Clawback provision*: The monitoring and clawback provision will ensure that if the beneficiary makes profits that are higher than initially foreseen in its investment plan, a proportional amount of the aid will be repaid so that public support is reduced to ensuring break-even within 36 months.

5.3. The distortions of competition and the effect on trade are limited, so that the overall impact of the measure is positive

- (36) The Commission concludes that the notified measure will offset a genuine geographical and commercial handicap of the targeted communes of Alto Adige and is objectively justified to address the lack of availability of broadband services therein on a purely market-driven basis. The target group of the scheme includes both local businesses and citizens who will benefit from the availability of broadband services in both their day-to-day business activity and in the quality of life benefits that access affords to citizens.
- (37) In view of the characteristics of the project and of the safeguards applied by the Italian authorities, the overall impact on competition is deemed to be positive. On the effect on trade, the Commission does not identify negative spill-over for other Member States.
- (38) On balance, the Commission concludes that the overall effect of the measure is positive. The measure is clearly in line with the objectives of Article 87 (3) (c) EC Treaty as it facilitates the development of certain economic activities (retail and, indirectly, wholesale broadband services) in certain remote and rural areas. The intervention is designed in a way that does not distort competition or affect trading conditions to an extent contrary to the common interest.
- (39) Finally, the Commission notes that the Italian authorities have provided a commitment to suspend the payment of the aid to companies that have not reimbursed or put on a blocked bank account any aid (including interests) which the Commission has decided to be unlawful or incompatible. As a result, the problem of the potential cumulative effect of the unrecovered incompatible aid with the notified aid, in application of the Deggendorf jurisprudence,⁸ does not arise.

5.4 Conclusion

- (40) In the light of the above, the Commission has come to the conclusion that the aid involved in the notified measure is compatible with Article 87(3)(c) of the EC Treaty.

VI. DECISION

On the basis of the foregoing assessment, the Commission has decided that the aid measure “Broadband connections for Alto Adige II” is compatible with Article 87(3)(c) of the EC Treaty.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

http://ec.europa.eu/community_law/state_aids/index.htm

⁸ Case C-355/95P, *Textilwerke Deggendorf GmbH (TWD) v. Commission* [1997] ECR I-2549, paragraphs 25-27.

Your request should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State Aid Greffe
Rue de Spa 3
B-1049 Brussels
Fax No: +32 2 2961242

Yours faithfully,

For the Commission

Neelie KROES
Member of the Commission