Action against Deutsche Telekom supports the development of competition in German broadband markets

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The European broadband markets are one of the key drivers of growth in the electronic communications sector. Experiences in the EU Member States show that competitive broadband markets lead to high broadband penetration which increases the competitiveness of the Member States and thus makes an important contribution to reaching the goals of the Lisbon agenda.

During the last years, the level of competition in the broadband markets of the biggest EU Member State Germany has been insufficient. The incumbent operator Deutsche Telekom (DT) has had well beyond 80% and thereby one of the highest shares in the EU15 retail broadband markets and an even higher share in the respective wholesale markets. In parallel, the broadband penetration in Germany has been relatively low and recently fallen behind the EU25 average for the first time. (1)

Besides the fact that there has only been minor competitive pressure from other broadband infrastructures (e.g. cable TV) and irrespective of the fact that DT has offered its competitors only a limited number of access forms to provide broadband services (2), the relatively low level of competition in the German broadband markets can above all be explained by DT’s anti-competitive behaviour as regards the access to its local loop. (3)

This is why the Commission has not only adopted its prohibition decision of 21 May 2003 against Deutsche Telekom (‘Deutsche Telekom’) (4) and subsequently concluded the so-called ‘QSC settlement’, but recently taken action against DT in order to safeguard the latter settlement, in which DT had committed itself vis-à-vis the Commission to terminate a presumed margin squeeze as regards broadband access.

Following this action, DT changed an application to the German telecoms regulator Bundesnetzagentur (BNetzA) (5) for the approval of wholesale fees it charges its competitors for shared access to the local loop (line sharing). BNetzA subsequently approved fees which are not only in compliance with the Commission’s action, but further improve the conditions for the provision of broadband services in Germany which had resulted from the initial ‘QSC settlement’.

The initial ‘QSC settlement’ and its implementation

Following an initiative from DT, in February 2004 DG Competition concluded a settlement with DT in a case which had been opened following a complaint by one of DT’s competitors in the German broadband markets, the Quality Service Communications AG (QSC). According to QSC, the margin between DT’s retail tariffs for ADSL and the corresponding wholesale tariffs for line sharing had been insufficient to allow new entrants to compete with DT on the retail market for broadband access. Such retail broadband access allows consumers to use a wide range of electronic communications services, such as high speed internet access and voice services entirely provided over the internet protocol.

The conclusion of the ‘QSC settlement’ followed a preliminary investigation that was based on the methodology for assessing a margin squeeze as developed in the ‘Deutsche Telekom’ decision. In that decision, the Commission had found that it is contrary to Art.82 EC if a vertically integrated operator (such as DT) which is dominant both on a wholesale and the related retail market(s) charges its competitors prices for wholesale access which are either higher than its comparable, weighted retail prices or if they are lower than those retail prices but insufficient to cover DT’s own product-specific costs for the retail service provision.

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(1) See Commission press release IP/05/642 of 1 June 2005.
(2) DT had not provided a DSL resale offer until mid 2004 and, according to preliminary findings of the German telecoms regulator Bundesnetzagentur, DT does not offer its competitors bitstream access yet.
(3) The local loop is the physical circuit between the customer’s premises and a telecommunications operator’s local switch. Its frequency spectrum can be split into a low frequency range for the provision of traditional voice telephony services, and a high frequency range enabling the provision of broadband access via xDSL. When both are rented out to new entrants, this amounts to full local loop unbundling, whereas the renting out of the mere high frequency range leads to shared access / line sharing. The wholesale line sharing fees are subject to the approval of the German telecoms regulator Bundesnetzagentur.
(4) OJ L 263 / 9 of 14 October 2003. See also Commission press release IP/03/717 of 21 May 2003. The decision is under appeal before the CFI as case T-271/03.
(5) The Bundesnetzagentur was previously known as Regulierungsbehörde für Telekommunikation und Post (RegTP). Its name was changed into BNetzA because the authority is now also regulating other network industries such as electricity, gas and railways.
On the basis of this methodology, DG Competition's services found indications that a margin squeeze existed also in the QSC case. To remove this competition concern, DT offered to terminate the presumed margin squeeze quickly and on a lasting basis, mainly by lowering its wholesale line sharing fees. Furthermore, DT committed itself to provide the Commission with all information to check that no margin squeeze would reappear.

Despite the fact that the 'Deutsche Telekom' decision could be seen as a precedent against DT, the Commission accepted these commitments in order to ensure that the presumed margin squeeze was terminated in a consumer-friendly manner (as it would not lead to higher retail prices) and in a competition-friendly manner (as it ensured that the presumed abuse could be terminated faster than by virtue of the adoption of a prohibition decision). Both factors were considered important in order to increase the level of competition on the broadband markets and ultimately broadband penetration in Germany.

After the conclusion of the settlement, market players were informed about its main points by way of a press release. (1)

Subsequently, DT undertook different steps to comply with the settlement and, above all, applied for substantially lower wholesale line sharing fees. (2) This application was accompanied by public declarations from DT that it intended to decrease its line sharing fees on a lasting basis in order to enable its competitors to develop the German broadband markets on an equal footing.

After BNetzA's approval of the reduced wholesale line sharing fees DT had applied for, the Commission was in a position to conclude that DT would lastingly comply with its commitments. The case was therefore closed in July 2004.

DT's new tariff application and DG Competition's reaction

While shared access had not taken up during the time when the presumed margin squeeze existed, i.e. before the conclusion of the 'QSC settlement', after its implementation some operators have publicly announced to roll-out their broadband infrastructure in order to provide retail broadband services on the basis of line sharing. According to press reports, first respective steps have been taken in early 2005.

At the end of May 2005, DT however filed an application to BNetzA in which it applied again for those line sharing tariffs which had caused the presumption of a margin squeeze during the Commission's investigations. DT's application was accompanied by press statements that the reduced line sharing tariffs would not have led to a market take-up so that DT would intend to charge the tariffs which had been applicable prior to the settlement again.

Based on the monitoring which has been set up for the German broadband markets in general and for DT's lasting compliance with its commitments in concrete, DG Competition's services could however presume that DT's application did not respect the settlement anymore. In order to prevent from tariff structures which would most probably have destroyed upcoming business models on the basis of line sharing, the Commission services therefore quickly intervened and asked DT either to provide the Commission with its calculations according to which the tariffs applied for would not lead to a margin squeeze or to withdraw its application and replace it by an application being in compliance with the settlement. This action was coordinated with BNetzA that had to decide upon DT's tariff application in August 2005.

After receiving the calculations on which DT had based its tariff application and on the basis of prior calculations it had provided, DG Competition's services were able to verify that DT's tariff application prima facie would lead to a margin squeeze and constitute a breach of the settlement. In order to avoid the opening of formal proceedings which might have led to the adoption of another Art.82-decision, DT was therefore required to submit an application to BNetzA that would be in compliance with its commitments. DT did so by re-applying for the monthly line sharing tariffs which had been approved as a result of the 'QSC settlement' in 2004.

Final implementation of the settlement on a lasting basis — BNetzA's role

At the beginning of August 2005, BNetzA finally approved monthly and one-off line sharing tariffs which were lower than the ones DT had finally applied for in order to comply with the settlement.
In this decision, BNetzA conducted a margin squeeze test by verifying in a first step whether the line sharing tariffs which could be approved on the basis of DT’s costs of efficient service provision would allow an efficient operator in the DSL retail market to compete profitably with DT. In a second step, BNetzA verified that these tariffs would also comply with the Commission’s margin squeeze test as set out in ‘Deutsche Telekom’, i.e. enable DT’s own downstream operations to trade profitably.

Although BNetzA’s ex ante tariff approval and its respective margin squeeze test was based on a forward-looking approach, it is interesting to note that BNetzA implicitly referred to both ways to assess a margin squeeze which are described in the ‘Access Notice’ (1), i.e. to focus (i) on the costs of the dominant undertaking and (ii) on the costs of an efficient competitor. While the Commission could already demonstrate / assume a margin squeeze on the basis of the more conservative option (i) in the ‘Deutsche Telekom’ decision and in the QSC case, BNetzA’s ‘cumulative approach’ in addition considers additional costs and less favorable economies of scale and scope of an efficient competitor.

By approving the new line sharing tariffs for two years, BNetzA has last but not least increased the certainty in the German broadband markets and ensured that the improved competitive conditions which resulted from the ‘QSC settlement’ will be secured on a lasting basis.

Against the background of positive experiences in other EU Member States such as France, it may therefore be expected that the improved conditions for the provision of broadband services via line sharing will lead to a significant market take-up and that they will positively influence the level of competition and penetration in the German broadband markets. In this context, it is worthwhile mentioning that the monthly number of fully unbundled local loops rented out to new entrants has no longer stagnated, but strongly increased after the implementation of the ‘Deutsche Telekom’ decision.

(1) Notice on the application of the competition rules on access agreements in the telecommunications sector, OJ C 265, 22.8.1998, page 2, no.117.