



EUROPEAN COMMISSION

Brussels, 8.X.2008
C(2008)5610 final

Subject: State aid N 248/2008 – United Kingdom
Direct International Communications Links into NW of Ireland (Project Kelvin)

Sir,

I. SUMMARY

- (1) I am pleased to be able to inform you that the European Commission has assessed the measure "*Direct International Communications Links into the NW of Ireland*" ("Project Kelvin") and decided not to raise objections as the State aid contained therein is compatible with Article 87 (3) (c) of the EC Treaty.

II. PROCEDURE

- (2) On 19 May 2008, the UK authorities notified the above mentioned measure¹. By letter dated 18 July 2008, the Commission requested additional information on the proposed measure.
- (3) By letter dated 19 August 2008, the UK authorities submitted their reply to the Commission's request of information.

III. CONTEXT AND MARKET SITUATION

Introduction

- (4) According to the UK authorities, the island of Ireland is growing in terms of its economy and its population but the pace of that change is uneven.

¹ An identical notification by the Irish authorities for the same Project was received by the Commission on 11 June 2008 (Case N 282/2008).

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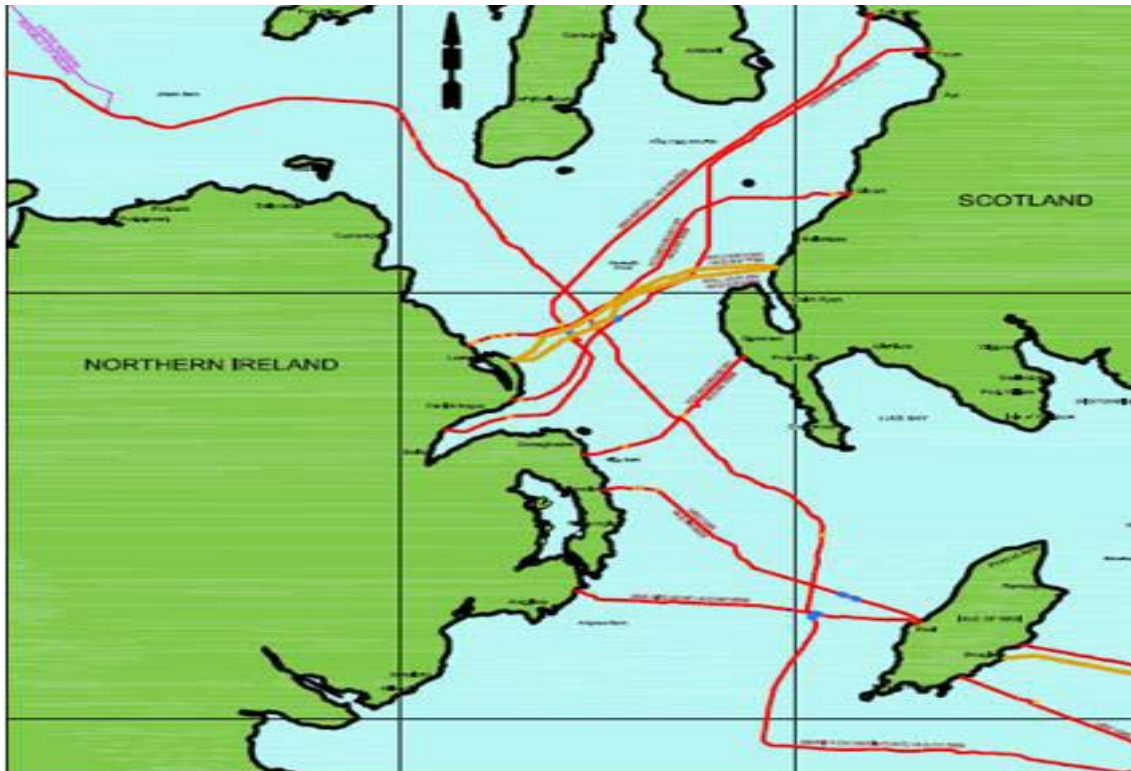
- (5) The North West of Ireland - which comprises parts of Northern Ireland and the Republic of Ireland - (the North West Gateway and the four Council areas of the City of Londonderry², Donegal, Limavady and Strabane), face issues common to both countries: (a) in terms of its economic prosperity relative to other parts of the island; (b) its relative isolation and distance from Belfast and Dublin (both actual and perceived), (c) its accessibility to key business and tourism markets; and (d) a need for improved and better co-ordinated services.
- (6) In order to assess the need for a co-ordinated development policy towards the whole of the North West of Ireland, in May 2006, during a meeting of the British Irish Inter-Governmental Conference (BIIGC), Ministers agreed to a North West Gateway Initiative (NWGI), comprising in particular a non statutory integrated spatial planning and development framework focussing on the Londonderry-Letterkenny gateway and the four local Council areas of Londonderry, Strabane, Limavady and Donegal.
- (7) According to the UK authorities, the development of this framework is significant in view of the identification of Londonderry and Letterkenny as key 'Gateway' areas both in Northern Ireland and in the Republic of Ireland, and the potential contribution that the accelerated development of the North West Gateway can make to the development of an arc of cities and other fast developing areas along the island of Ireland's western coastline and to complement and counterbalance the existing strong metropolitan corridor from Belfast to Dublin.
- (8) According to the UK authorities, the "North West Direct International Connectivity Project" ("Project Kelvin") will contribute to the above described objectives of both the British Irish Inter Governmental Conference and the North West Gateway Initiative.

Existing international connectivity in the island of Ireland

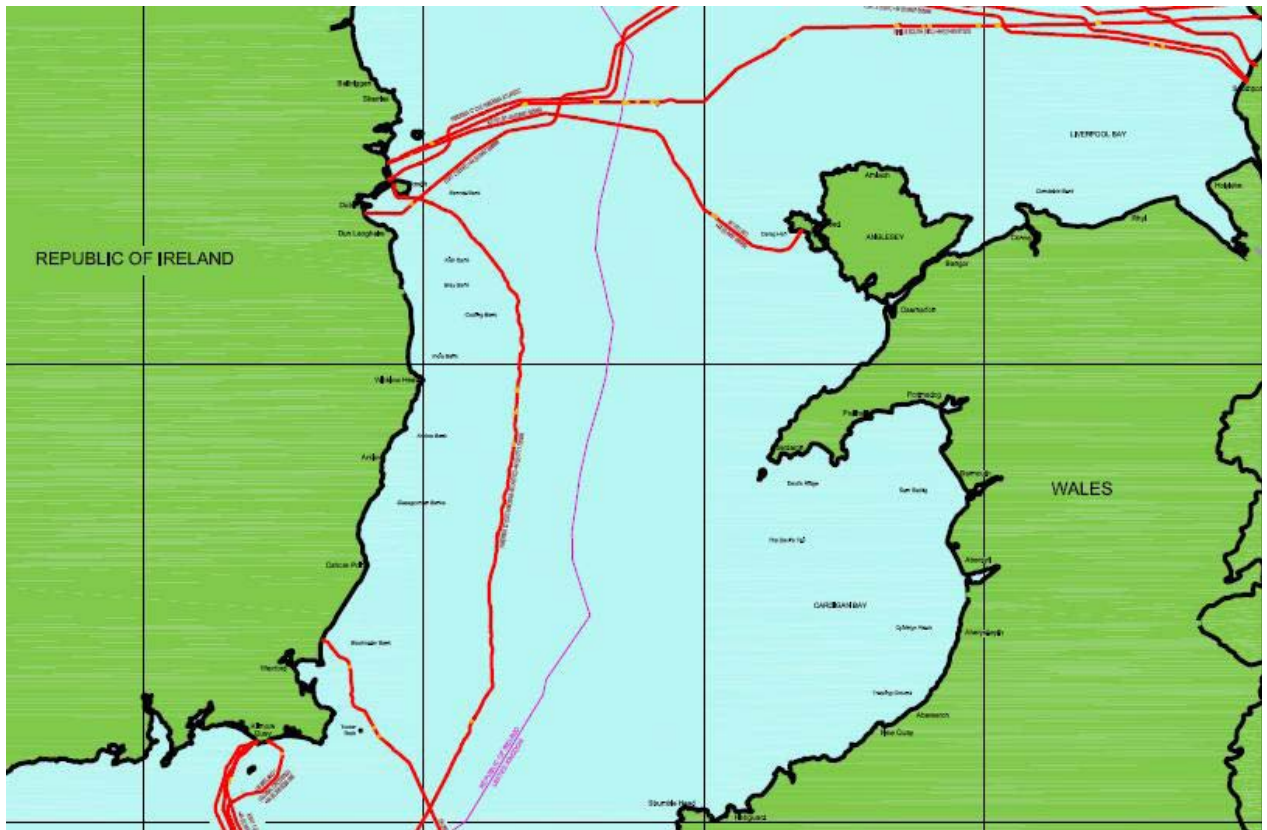
- (9) There are two methods of providing international connectivity to an island: submarine cables and satellite systems. Satellite systems are traditionally more expensive for the end consumer and introduce increased latency when compared to submarine systems. Submarine cable systems are the connectivity of choice for inter-continental, long-distance and large volume island regions.
- (10) According to the UK authorities, both jurisdictions within the island of Ireland are completely dependent on submarine telecommunications links for international connectivity. Northern Ireland relies on submarine cable links to the British mainland, whereas the Republic of Ireland relies on a combination of submarine links to Britain and direct international links into Dublin and Wexford. All of these existing submarine cables in both jurisdictions are located on the east and south coast of Ireland.

² Different naming conventions have been used by the Irish and UK authorities in their respective notifications of Project Kelvin. Thus, the same city is referred to as "Londonderry" by the UK authorities and "Derry" by the Irish authorities. The Commission decision in each notification adopts the name convention used therein.

- (11) In particular, as far as Northern Ireland is concerned, there are currently six submarine cables connecting Northern Ireland to international exchanges in Great Britain. Three of these belong to BT, two to Cable & Wireless and one to NTL-Telewest. All of these cables are located on the east coast of Northern Ireland and cross the Irish Sea to Britain via Scotland, Isle of Man or England. Both the control of these cables and their locations has a significant impact on the range and costs of telecommunications services available in Northern Ireland and the North West region.



- (12) There are nine submarine cables providing international connectivity for the Republic of Ireland, eight of which connect via Great Britain. All of these existing cables are in the Dublin or Wexford region (east and south coast) and connect to the Wales, the Blackpool area or the Devon/Cornwall region of England. These are controlled by four operators. There is one submarine cable which connects the Republic of Ireland directly to North America from Dublin, while the others are switched through Great Britain onto trans-Atlantic cable systems. County Donegal, although geographically closer to Northern Ireland, connects back to Dublin for its international connectivity as do other parts of the border Region.



The inland telecommunications market and the demand for international connectivity

- (13) Among other things, the implementation of any international connectivity projects requires an appropriate terrestrial telecommunications infrastructure capable of providing the international link traffic and customers in order to use the available capacity.
- (14) Five network providers are present in Northern Ireland (BT, NTL, Bytel, eircom and Cable Wireless). The existing terrestrial infrastructure within the region is quite extensive and with many high-bandwidth routes around it. BT' fibre network is the most extensive due to its position as the incumbent operator. It connects to the Republic of Ireland via Newry (on the east), and its own submarine cables to the UK. All existing operators are in the process of upgrading their infrastructure in order to handle the increased traffic and the higher bandwidth requirements for new services by deploying full fibre ring networks. Therefore, it is envisaged that there will be ample terrestrial infrastructure to which the international cable can connect to.
- (15) As far as demand is concerned, there are four key sectors that will drive demand for international connectivity. These are the SMEs, the Corporate Sector, Media and Broadcasting, and to a lesser extent, the Residential sector. The UK authorities have provided data showing that currently, for business consumers 25% of the traffic goes to North America and the remaining 75% to Europe and other continents. With Project Kelvin, traffic to North America is expected to increase by 44% given the continuous growth of new, bandwidth-hungry internet applications and the deployment of Next Generation Networks.

In particular, the need for international connectivity in the NW of Ireland

- (16) The UK authorities emphasise that companies in the North West are at a competitive disadvantage as a result of the physical peripherality of the region, its distance from the international telecommunications links and the lack of competition in the North West region telecommunications market. The region encompasses two jurisdictions with distinctly different telecommunications networks. The existence of the border causes markets to fragment along territorial lines, reducing economic interaction and the opportunity to develop economies of scale and strong indigenous industries. Infrastructural links are not developed as witnessed by the separate and barely linked existing networks in the two border jurisdictions, resulting in unbalanced economic growth.
- (17) The fact that the North West region contains an international border explains why there is no regulation of the electronic communications markets between Northern Ireland and the Republic of Ireland (the UK part of the region is regulated by OFCOM, the Republic of Ireland part by ComReg). As a result, there are considerable differentials in telecommunications costs between locations within a few kilometres of each other but separated by the border.
- (18) The cost disadvantages become clear when the costs for companies in London or Dublin are compared to the costs faced by companies in the North West of the island of Ireland. In this respect, the UK authorities refer to a feasibility study on Direct International Connectivity for the North West region compiled in 2007 by PA Consulting according to which the cost of high speed broadband from Dublin to London or Dublin to New York is around £ [...] * per Megabit (Mb) per year. For companies in London the cost per Mb to New York is also in the region of £ [...] per year. However, companies in Northern Ireland face the additional cost of backhaul to Dublin or London. For companies in the largest city in Northern Ireland, Belfast, the cost for backhaul to London is £ [...] per Mb per year and to Dublin £ [...] per Mb/year. For companies in the North West, for example in Londonderry, there is the additional cost of backhaul to Belfast which can be up to £ [...] per Mb/year.
- (19) Likewise, while the total cost for a company in London or Dublin for backhaul to the North American telecommunications hub in New York is £ [...] per year Mb, for a company in Londonderry in the North West of the island of Ireland, the cost of direct international connectivity to New York can be in the region of £ [...] per Mb/year and more (backhaul to Belfast £ [...] per Mb), backhaul from Belfast to London £ [...] or Belfast to Dublin £ [...], and finally the cost of backhaul to New York £ [...] The position is the same for connectivity to mainland Europe as companies in the North West still have the extra backhaul costs to Dublin or London before they can reach the European telecommunications hubs.

IV. DESCRIPTION OF THE MEASURE (PROJECT KELVIN)

- (20) The proposed project aims to bring a direct international link through a new submarine telecommunications cable into the North West of Ireland. At present there are no direct international links into the North West. The nearest direct international links from the island of Ireland are in South East in Dublin. The new cable is expected to be

* Business secret.

connected to an existing transatlantic cable in a way that will provide direct international connectivity into the North West.

- (21) In practice, a direct international link to North America can be achieved in three ways: (i) a transatlantic cable which lands on the island of Ireland, (ii) a spur taken from a transatlantic cable (for example from North America to the UK) where the spur lands on the island of Ireland, or (iii) a submarine cable from the island of Ireland which joins with a transatlantic cable at its landing point. By contrast, submarine links from the island of Ireland which land in England, Scotland or Wales and use terrestrial infrastructure including switches to interconnect with the transatlantic cable systems are considered to be indirect international links.
- (22) The UK authorities point out that the cost of the most recently constructed transatlantic cable network (the two Hibernia North and south cables - Nova Scotia, Canada to Dublin, Ireland in 2000) was \$850m. To date, it is estimated that the cost for a single cable linking North America to Ireland at 2008 prices would be around \$250m. The feasibility study carried out by PA Consulting for Project Kelvin confirmed that there is still spare capacity available on some of the existing transatlantic cables (although none of these land in the North West) and therefore no incentive for the private sector to build a new transatlantic link. The study also reported that it would be possible to achieve a direct international link into the North West by connecting to an existing transatlantic cable. The PA Consulting report identified the Hibernia North cable, some 30Kms off the north coast the island of Ireland, as the most cost effective way of achieving a direct international link for the North West since building a completely new transatlantic cable is prohibitively expensive. However, there is nothing in the tender for Project Kelvin to stop the private sector from proposing this solution.
- (23) The UK and Irish governments have committed to organise a tender as the best way of testing the market and giving the private sector the opportunity to develop the most appropriate solution for the North West.
- (24) The UK authorities add that the private sector has not invested in providing direct international connectivity to the North West region nor are there any indications that it will do so in the future, the main reason being that the North West region of both Northern Ireland and the Republic of Ireland are the most distant from the existing submarine cables and the international exchanges they serve.
- (25) In particular, Project Kelvin will require a new direct link to the transatlantic submarine telecommunications networks. The cable will come ashore on the north coast of the island of Ireland. Both the Irish and the UK governments have agreed that Londonderry is the most suitable location for the direct link to terminate. The new direct link will also be able to interface with the existing Northern Ireland telecommunications infrastructure (BT, NTL, eircom and others) in Londonderry.
- (26) To remove the impact of the border and ensure that the benefits of project are made available as widely as possible, two locations within the Republic of Ireland will also gain access to the new direct international link, Letterkenny and Monaghan.³

³ More particularly, the infrastructure to be built comprises not only a submarine but also a terrestrial infrastructure. The terrestrial infrastructure comprises, as a minimum, a Telehouse facility to be built in

Letterkenny is in Donegal, and 37 km from Londonderry. Monaghan is even further, 108 km from Londonderry and less than 20 km from the border and Northern Ireland's core telecommunications infrastructure. As a condition of Project Kelvin, access to the direct international link will have to be available at the co-location centres on both towns' Metropolitan Area Networks. The same range of telecoms services and associated costs will be available at Londonderry, Letterkenny and Monaghan.

- (27) The UK authorities have also confirmed that the owners of existing submarine cables were consulted about Project Kelvin (BT, C&W, NTL/Telewest, Hibernia Atlantic, Global Crossing) and presentation were also made to other submarine cable operators who have expressed an interest in entering the NW region market.
- (28) The UK authorities add that in December 2007, [a network operator – confidential] indicated to the Department of Enterprise, Trade and Investment its opposition to the proposed direct international connectivity project. [The network operator-confidential] acknowledged that it imposes distance related charges on companies outside Belfast, but stated that this would be changed in the future to a system where charges would be based on distance from their main telecoms switches in [...]. [The network operator – confidential] subsequently confirmed that the new prices for a 2Mb MPLS⁴ link to New York in the following locations within the INTERREG IVA area⁵ are as follows:
- *Northern Ireland locations*: within 40Km of Belfast, Londonderry and Portadown: € [...] yearly rental.
 - *Irish Republic locations*: Letterkenny (37Km from Londonderry): € [...] yearly rental, Monaghan (46km from Portadown): € [...] yearly rental.
- (29) The UK authorities also provided information given by the Irish government in relation to the prices applied by [a network operator- confidential]. Thus a 2 Mbit/s MPLS link from Letterkenny to New York costs € [...] per year, and from Monaghan to New York € [...] per year.
- (30) In their reply to the Commission request for further information [see above para.(3)], the UK authorities stated that [the network operator's- confidential] revised prices for the services in Monaghan and Letterkenny are still higher than in Londonderry as the existence of the border continues to adversely impact on price. The revised prices are also higher in all parts of the North West (including Londonderry) than in Dublin,

Londonderry and diverse connections between the Telehouse and the Co-locations Centres of the existing MANs in Letterkenny and Monaghan. The submarine infrastructure will include a new submarine cable that will link the terrestrial infrastructure to one or more suitable transatlantic submarine cables at a specified landing point to be located along the coast of County Antrim or County Londonderry (both in North Ireland).

⁴ Multi Protocol Label Switching.

⁵ The INTERREG IVA Programme is the Cross-Border Territorial Cooperation Programme for Northern Ireland, the Border Region and Western Scotland. The INTERREG IVA Programme (2007 – 2013) is targeted at the following eligible NUTS III areas: (i) North of Northern Ireland; East of Northern Ireland; West and South of Northern Ireland; (ii) the six necklace counties along the border with Northern Ireland i.e., Cavan, Donegal, Leitrim, Louth, Monaghan and Sligo; and (iii) in Scotland: Lochaber, Skye & Lochalsh, Arran & Cumbrae and Argyll & Bute, Dumfries and Galloway, East Ayrshire and North Ayrshire mainland, and South Ayrshire.

Manchester and Glasgow for a comparable service.⁶ By contrast, the pricing mechanism proposed as part of Project Kelvin aims to ensure that pricing in Londonderry, Letterkenny and Monaghan is in line with prices in Dublin, Manchester and Glasgow. According to the UK authorities, [the network operator – confidential], like any other commercial operator, can freely change its prices for international connectivity (up or down) depending on its perception of the market. To date, that has meant higher prices for international connectivity in the North West than available from other operators in, for example, Dublin, Manchester or Glasgow where there is much greater competition in the international electronic communications market. The UK authorities emphasize that the project also aims to improving latency and resilience as well as increasing competition in the relevant market. The reductions in [the network operator's – confidential] pricing are not therefore enough to achieve the aims of this project although they are seen as a welcome move in the right direction⁷.

- (31) Moreover there are comparably few cross border links between the Northern Ireland and Irish Republic telecoms networks other than on the east coast between Belfast and Dublin. In the North West the only links between the networks are two fibre optic links (1Gb plus) between Londonderry to Letterkenny - one belonging to BT and the second belonging to eircom, the Irish fixed-line incumbent operator. According to the UK authorities, the two links from Londonderry to Letterkenny have improved connectivity in Letterkenny and increased opportunities for cross border collaboration and also improved competition in that both BT and NTL/Telewest are now operating in the Donegal area. However, the border continues to adversely impact on prices (prices are much lower in Londonderry than in Letterkenny). Compared to Dublin or cities like Manchester or Glasgow in the UK, prices in the NW for international connectivity remain very high. The new links have not reduced latency in line with or below the requirements specified for Project Kelvin. This is mainly because they use the existing land based infrastructure and either the indirect submarine links to the UK mainland or via Dublin. There remain many switching points between the NW and a direct international link. Moreover, the two links have not increased the resilience of the island's international infrastructure as they rely on the existing submarine cables.
- (32) The UK authorities consider that Project Kelvin should not have a significant negative impact on the existing cross border links. Companies bidding for Project Kelvin will seek to use the existing cross border links to get diverse and resilient links from the Telehouse facility in Londonderry to Letterkenny and Monaghan. Only in the event that a commercial deal could not be reached with the owners of the existing links would a bidder consider building a new cross border link. In addition, BT's cross border link was built to allow BT to service its Donegal customers in the republic of Ireland using its own infrastructure rather than rely on other companies infrastructure or wireless links. Project Kelvin will not change that requirement. Likewise, the BT link to Letterkenny gives BT access to the Metropolitan Area Networks (MAN) and is therefore part of its strategic infrastructure. With regard to eircom's cross border link, the UK authorities note that eircom had telecoms ducts in place for approximately half the distance from Letterkenny to Londonderry (the ducts stopped just short of the

⁶ According to the UK authorities, the wholesale price of a 2 Mb E1 connection from Dublin to New York can be as low as \$411 per month (\$4932 per year), see *Telegeography Bandwidth Report* 23 June 2008.

⁷ [A network operator – confidential], another company which operates in the Irish market, has quoted the following prices: for a 2 Mb MPLS link from Letterkenny or Monaghan to New York (excluding installation): € [...] per year € [...] Letterkenny or Monaghan end and € [...] at the New York end).

border) for many years. The additional infrastructure (ducts and cables) to connect Letterkenny to Londonderry was installed only in recent years because eircom needed to improve the resilience of its network in Donegal. Project Kelvin will not remove the need for this.

- (33) The main aspects of Project Kelvin can be summarised as follows.
- (34) *Objective:* The objectives of Project Kelvin are: (i) to bring a *direct* international telecommunications link into the North West region of the island of Ireland, (ii) to increase competition in the North West telecommunications market especially for the provision of international telecommunication services, (iii) to make the cost of international telecommunication services within the region the same as in main urban areas in the United Kingdom and the Republic of Ireland, (iv) to provide access to direct international communication services to businesses, particularly to Small and Medium Enterprises (SMEs) located within the region, (v) to reduce latency between the North West and North America and mainland Europe, and (vi) to increase the resilience and diversity of the telecommunication's infrastructure in the North West region.
- (35) *Legal basis:* Project Kelvin is a joint project by the Department of Enterprise, Trade and Investment Northern Ireland (DETI-United Kingdom) and the Department of Communications, Energy and Natural Resources (DCENR-Ireland) under the Northern Ireland, Border Region and Western Scotland INTERREG IVA 2007-2013 programme. The overall aim of the INTERREG IVA programme is to 'support strategic cross border co-operation for a more prosperous and sustainable region'. In the UK, the legal basis is the "Communication Act 2003".
- (36) *Maximum aid amount and intensity* The overall expenditure planned by DETI and DCENR is €30 million (£24,63 million). The total value of the combined public and private sector investment will not however be known until the tender process has been completed. The maximum aid intensity is 75% of the total cost to the public sector.
- (37) *Funding instrument:* The INTERREG IVA programme will provide 75% of this overall expenditure and the balance by the UK and Ireland governments.

Funding source	United Kingdom	Ireland	Total
European Regional Development Fund	€16.29m	€6.21m	€22.5m
National	€4.5m	€3m	€7.5m
Overall totals	€20.79	€9.21	€30m

- (38) *Beneficiaries:* The direct beneficiaries of the aid will be the successful operator(s) that will build and own the direct link and any other associated infrastructure. Indirect beneficiaries will be third party providers of electronic communications networks and services, and business end-users located in the North West region of the island of Ireland. The provider will sign a contract for ten years.

- (39) *The selection procedure:* The aid will be granted by means of an open procurement tender process in compliance with the applicable EU legislation. The tender process will be managed jointly by the DETI (Northern Ireland) and the Minister for Communications, Energy and Natural Resources (Ireland).
- (40) *Selection Criteria and other specifications:* The two governments have issued a detailed tender documentation in which the requirements for Project Kelvin including the main performance specifications (i.e., resilience, latency, submarine and terrestrial infrastructure) and the evaluation criteria are clearly described. Although the technical performance that the new direct international link must meet are specified, the evaluation criteria will reward bids which exceed the minimum specification, for example latency. Three mandatory locations are included in the tender (Londonderry, Letterkenny and Monaghan), but the evaluation mechanism encourages bidders to give access to additional towns and cities within the area covered by INTERREG.
- (41) *Services provided and Product Pricing:* The range of agreed telecommunication services and price at each access points in the North West region of the island of Ireland must be the same as in the main Ireland and UK urban centres of Glasgow, Manchester and Dublin ("benchmark product pricing").⁸ The telecommunications services specified in the tender documentation will have to be available at the very least in Londonderry, Letterkenny and Monaghan on the same terms and conditions.⁹
- (42) *Wholesale access:* The mandatory pricing mechanism specified in the tender is based on wholesale prices for the mandatory products offered at international exchanges in Dublin, Manchester and Glasgow. The cost to the end user, whether a telecoms or non telecoms company, cannot exceed the benchmark price set through the pricing mechanism. This pricing mechanism will operate for the duration of the contract (10 years). In addition, access to the direct international link in all mandatory locations is carrier neutral in the sense that any type of company can have access on equal terms.
- (43) *Duration of the measure:* The scheme runs from 2008 until the end of 2018
- (44) *Monitoring:* Although the direct link and any associated infrastructure will be owned and managed by the private sector, the contract signed will include arrangements for monitoring both the price of connectivity offered and the level of service on a yearly or more frequent basis.
- (45) *Revenue sharing:* The contract will also include revenue sharing conditions to protect the public sector investment in the event of windfall gains. In particular, in consideration for the aid granted, the contracting authorities will be entitled to receive 37,5% of the "Excess Annual Revenue" (as defined in the contract) and will also be entitled to benefit from any increase in the value of the core assets to of the infrastructure to be built during the 10-year contractual term.

V. OFCOM'S AND COMREG'S COMMENTS

⁸ The benchmark product pricing will be based on the lowest of the median prices available for each product in each of the three cities (Glasgow, Manchester, and Dublin).

⁹ These services will include for example, client access in each of the three locations at 2, 10 and 45 Mb, STM-1, STM-4, STM-16, STM-64, 1GE, 10 GE (LAN PHY) and direct wavelength access.

- (46) The Department of Enterprise, Trade and Investment informed the Office for Communications (OFCOM, the UK regulatory authority) about Project Kelvin in June 2007. In its reply, OFCOM raised no objections to the project. It recalled the principle that any public sector organisation seeking to intervene in the provision of communications infrastructure must ensure compliance with state-aid rules. For OFCOM, where there are potential market failures at some points in the value chain, State interventions can promote competition or consumer benefits. Examples include schemes aimed at bringing lower cost middle-mile connectivity to business parks that may increase the take-up of higher bandwidth services by businesses, or reducing the cost of backhaul links to exchanges in order to facilitate investment in local loop unbundling by new entrants.
- (47) ComReg, the Irish regulatory authority for electronic communications, considers that the fibre link of Project Kelvin when connected to the Irish national electronic communications network in Monaghan and Letterkenny would fall into the ex ante regulated market for "International Retail Leased Lines". There currently exists a significant level of international connectivity in this market, which was deemed to be competitive in December 2004 (ComReg document 04/120). Thus, ComReg will have no regulatory concern regarding Project Kelvin.

VI. ASSESSMENT OF THE MEASURE: PRESENCE OF AID

- (48) According to Article 87 (1) of the EC Treaty, "*any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market*". It follows that in order to be qualified as State aid, the following cumulative conditions have to be met: 1) the measure has to be granted out of State resources, 2) it has to confer an economic advantage to undertakings, 3) the advantage has to be selective and distort or threaten to distort competition, 4) the measure has to affect intra-Community trade.

VI.1. State resources

- (49) The measure is financed by resources by the UK government with co-financing by the ERDF (INTERREG IVA). Hence, State resources are involved.

VI.2. Economic advantage

- (50) *Selected operator*: the selected operator to build, and maintain the submarine cable will receive financial support which will enable it to enter the market and provide international connectivity in the NW region of the island of Ireland on conditions not otherwise available on the market. The selected operator will also be in ownership of the infrastructure thus built after the lifetime of the 10-years contract signed, and will thus enjoy benefits partly funded with State resources after the end of the project. In view of the above, it is clear that an economic advantage will be granted to the successful bidder.
- (51) *Third party providers*: In the area covered by the project, there is no direct international connectivity available. Existing electronic communications network providers need to buy backhaul capacity and international connectivity from submarine cables located further away in the east (Belfast) and south east (Dublin)

costs of the island of Ireland at much higher costs than operators that are closer to better connected areas such as Dublin, London, Manchester or Glasgow do. Therefore, third party interconnecting with the three access points of the infrastructure to be built (Londonderry, Letterkenny, Monaghan) will get lower, non-distance related backhaul connectivity prices. Business end-users will also benefit from the expected lower costs for their connectivity needs as well from the provision of better and more resilient electronic communications services with a lower degree of latency.

VI.3. Selectivity and distortion of competition

- (52) The notified measure supports the supply of direct international connectivity in the North West region of the island of Ireland. The intervention of the State alters the existing market conditions by allowing the provision of direct international connectivity services by the selected operator and the provision of electronic communications services by third party network providers. A number of undertakings are likely to subscribe to the services provided by the owner of the new submarine cable instead of more expensive satellite services or the current, equally expensive and distant-related products that are offered at the submarine landing points in Belfast and Dublin. Therefore, the fact that a new direct international connectivity will enable the provision of electronic communication services in the NW region of the island of Ireland at lower prices than existing ones has the effect of distorting competition.
- (53) In addition, while the UK and Irish authorities decided jointly to intervene precisely in view of the lack of private initiatives in the targeted area, it cannot be excluded that market initiatives could become viable in the longer term. By securing this project, the chosen operator will be capable of establishing its business and developing its customer base, enjoying a first mover advantage over prospective submarine cable competitors aiming to serve the NW of the island of Ireland.
- (54) The measure is also selective in that it is addressed to undertakings active only in certain markets for electronic communications services. This selectivity element also induces a potential distortion of competition¹⁰.

VI.4. Effect on trade

- (55) 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 is also an effect on trade between the businesses that require international or cross-border connectivity and their competitors in other Member States.

VI.5. Conclusion

- (56) In view of the above, the Commission considers that the projects covered by the notified measure will grant an economic advantage to the selected submarine cable operator and possibly to third party operators. The project is publicly funded, has a potential of distorting competition and has an effect on trade between Member States.

¹⁰ As regards the sectoral specificity, see for instance Case C-143/99 *Adria-Wien Pipeline and Wietersdorfer & Peggauer Aementwerke* [2001] ECR I-8365.

Therefore the Commission considers that the funding covered by Project Kelvin involves State aid within the meaning of Article 87 (1) of the EC Treaty.

- (57) Having established that the project involves aid within the meaning of Article 87(1) of the EC Treaty to the selected submarine cable provider, third party providers and businesses, it is necessary to consider whether the measure can be found to be compatible with the common market.

VII. ASSESSMENT OF THE MEASURE: COMPATIBILITY

- (58) The Commission notes that the project aims to bring a direct international submarine cable connectivity into the North West region of the island of Ireland in order to make the costs of international electronic communications services within the region the same as on the main urban areas in the United Kingdom and in Ireland, with no prospect for such connectivity being secured on commercial terms in the near and medium term, and as such, does not fall under any of the existing frameworks and guidelines.
- (59) It should be noted that although some of the areas covered by the measure could be eligible to receive regional investment aid under the derogation of Article 87(3)(a) or (c), the same cannot be said in respect of its impact on the third party network operators and business end users for whom the benefit is not linked to any initial investment.¹¹
- (60) 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 Treaty¹² which states that:

“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.

- (61) 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 particular, the measure shall be assessed with respect to 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?

¹¹ See "Guidelines on national regional aid for 2007-2013", OJ C 54, 4.3.2006 and Commission decision in case N 459 / 2006 – "German regional aid map 2007-2013" OJ C 295. 5.12.2006.

¹² This approach was also followed by the Commission in other similar cases that involved support for the roll out of broadband infrastructure in underserved areas, see for instance: State aid decisions for cases N 442/2007 "Aid in favour of broadband in remote areas of Veneto", Italy of 23.10.2007 or N 570/2007 "Broadband in rural areas of Baden-Württemberg", Germany of 23.10.2007 or N 14/2008 "Broadband in Scotland – Extending broadband reach", United Kingdom of 30.04.2008.

- (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?

VII.1. The support for direct international connectivity is in line with the common interest

Market failure and cohesion considerations

- (62) There is clear evidence that in general, the development of an electronic communications infrastructure is critical to a country's macroeconomic development and competitiveness. For peripheral island regions an expanded electronic communications and broadband infrastructure can play a central role in their economic development.
- (63) In this respect, the provision of submarine international connectivity is essential for islands and their regions as it is in essence the only way to interconnect with other continents and establish thus secured and resilient electronic communications links. In particular, the choice of landing of a cable ashore is critical as it determines the backhaul connectivity costs for the users of such infrastructure. Clearly, submarine cables land on or close to important urban areas which are densely populated, are important centres of economic activity and have a clear need for affordable international communications links. By bringing submarine connectivity near such areas, interconnection and backhaul costs are greatly reduced for users in these areas. Moreover, international submarine connectivity is inextricably linked with the provision of broadband services as internet traffic crosses borders and continents to connect users and provider of e-services. Today, there is clear evidence that regional economic development results not only from greater broadband deployment but also from affordable broadband services, including increased efficiency, productivity and welfare gains. Without affordable, secure, and resilient international connectivity, island regions cannot benefit fully from broadband services. In that sense, international submarine connectivity landing on rural and peripheral region of an island can have a positive effect of the deployment of affordable broadband services in the region in question while at the same time contributing to increasing the overall international connectivity links of the island as a whole.
- (64) It appears that for island regions, the lack of adequate international submarine cable connectivity is due, among other factors, to some of the typical economic problems associated with networks industries, in general. In particular, due to economics of density, it is more profitable to land submarine cables on areas where there already exist adequate telecommunication networks to connect to and where actual or potential demand for international electronic communication services is higher and concentrated, i.e. in densely populated areas. It is not therefore a coincidence that all submarine cables connecting directly or indirectly the island of Ireland with mainland Europe and other continents land on the two main cities, Dublin and Belfast. Both cities are indeed the main economic hubs in the Republic of Ireland and Northern Ireland, respectively.

- (65) To date there is no direct international connectivity in the North West of the island of Ireland whose overall economic development is lagging behind in comparison with other more prosperous areas of the island, such as Belfast and Dublin which have created and benefit from a strong metropolitan corridor along the north-east, south-east coast of Ireland. Moreover, the existence of a border creates additional barriers to the economic development of the region as the existing electronic communications infrastructure in the area is subject to two separate jurisdictional regimes. As a result, for instance, Irish business users that may be located closer to the border and the Belfast area will still have to pay more for their international connectivity needs as they need to buy ("longer") backhaul capacity in order to interconnect with the submarine cables located further away in Dublin.
- (66) Project Kelvin will bring international connectivity in at least three main towns currently separated by the border (Londonderry, Letterkenny and Monaghan) and ensure that, despite the existence of a border, electronic communications services will be provided on the same terms and conditions, irrespective of the actual distance from the landing point of the cable, thus reducing the distance and border-related handicaps of the whole region.
- (67) Thus, by jointly proposing to bring a direct international submarine communication link to the North West region of the island of Ireland, the UK and Irish authorities pursue genuine cohesion and economic development objectives.

VII.2. Well-designed aid

(a) Aid is the appropriate instrument

- (68) The measure at hand is part of an overall joint strategy of the Irish and UK governments to increase the competitiveness of the NW region of the island of Ireland in order to promote regional development and allow services to operate more easily across border by encouraging (new) electronic communications operators to enter the market and thus stimulate improved choice, quality and pricing of electronic communications services to end users and in particular to businesses with increased data connectivity needs.
- (69) Project Kelvin is also aimed to bring cross-border benefits through improved communications routing (resilience and security of supply), network availability and capacity. Given the existence of the border, such benefits cannot be realised by market forces alone. The electronic communications networks present in the NW region are subject to two separate jurisdictional and regulatory regimes and neither the market for the provision of international connectivity is subject to ex ante regulation in any of the two countries concerned. Given the particular characteristics of the NW region of Ireland, there is no alternative to granting public funding to overcome the economic barriers due to the existence of a border, and the lack of direct international submarine connectivity in the region.
- (70) In view of these considerations, the Commission concludes that, in the case at hand, public funding for the realisation of Project Kelvin is an appropriate instrument to achieve the set objectives.

(b) The aid provides the right incentives to operators

- (71) As explained above, the recipient of the aid will be selected by means of an open public tender in which bidders will have to submit their investment plans indicating the amount of aid that they consider to be necessary to bring direct international connectivity in the NW region of the island of Ireland as well as how many cities outside Londonderry, Letterkenny and Monaghan they would be ready to interconnect. Therefore, the State aid measure provides a direct and appropriate investment incentive limited to the amount required by the selected bidder.

(c) Proportionality

- (72) The UK and Irish authorities have designed Project Kelvin in a way which minimise the State aid involved and the potential distortions of competition. In this respect, the Commission notes the following positive elements in the overall design of the measure:

- (a) *Market analysis and consultation of operators:* The UK and Irish authorities have carried out an extensive market and feasibility study in order to analyse the costs of bringing a direct international telecommunications link into the NW region of the island of Ireland, by analysing in particular the capital infrastructure costs to connect such a system to the existing inland infrastructure. They have also examined which is the most suitable landing point that could maximise the success of the cable connectivity in terms of collocation and interconnection requirements. The contracting authorities have also consulted all existing submarine operators as well as potential new entrants in order to gauge their interest and intentions to provide themselves the required connectivity. They have also analysed the costs of backhaul connectivity for business users and other alternative possible options that could also meet the international connectivity needs of the region. In that sense, the aid granted is based on a prior assessment of the economic rationale and of the need for funding a direct international submarine connectivity link.
- (b) *Transparency and open Tender:* The aid will be granted on the basis of a transparent and open tender, in full compliance with the existing EU procurement rules. A contract will be concluded with the bidder having submitted the most economically advantageous offer, being the bidder that receives the highest marks in accordance with detailed and pre-defined published award criteria.
- (c) *Carrier neutral:* The scheme is carrier neutral, in the sense that any company could be connected to it, be it an electronic communications operator or not.
- (d) *Services and type of access provided:* The selected operator will have to grant network access to any third party on the same terms and conditions (equal and non-discriminatory access). In this respect, the contracting authorities have specified a list of minimum mandatory services to be provided to third parties covering access products from 2Mbit/s to 10 Gbit/s Direct Wavelength Access. Coupled with increased latency, resilience and availability (99,999%) requirements imposed on the successful bidder, the new international submarine connectivity link should stimulate entry in the region by third party access seekers, thereby strengthening choice and competition in the region.
- (e) *Minimisation of price distortion:* The selected operator will have to offer services at prices that are comparable to the average prices of the same products available from

other service providers in Glasgow, Manchester and Dublin. The existence of a competitively priced infrastructure that will emerge from Project Kelvin will encourage new operators to enter the North West market to the benefit of end-users.

Finally, Project Kelvin is not going to negatively affect existing operators in the North West of Ireland to an extent that is contrary to the common interest. Prices for international connectivity remain very high given the international backhaul connectivity costs involved. As the UK authorities have confirmed, the revised prices of BT for the services provided in Monaghan and Letterkenny are still higher than the prices in Londonderry as the existence of the border continues to have an adverse impact on price. The revised prices in question are also higher in all parts of the North West than in Dublin, Manchester and Glasgow for a comparable service. Moreover, the revised prices of BT do not address the objectives of increased latency and resilience sought by the realisation of Project Kelvin.

With regard to the cross-border networks links already built by BT and eircom, as the UK authorities have explained, Project Kelvin is not going to have an adverse effect to an extent that is contrary to the common interest. BT's cross-border link was built to allow BT to serve its own customers in the Republic of Ireland (Donegal) without having to rely on third party infrastructure. Project Kelvin will not change this requirement. Nor is the connection between Letterkenny and Londonderry recently built by eircom in order to improve the resilience of its network in Donegal going to be rendered redundant or adversely affected by Project Kelvin. In fact, eircom could also seek to interconnect its cross-border links to any of the three mandatory access point locations in the North West (Londonderry, Monaghan, Letterkenny) in order to lower its own international backhaul costs and compete more effectively with other network providers in the region.

- (f) *Monitoring and revenue sharing mechanism:* The project will be examined on regular basis by the two granting authorities which will also be entitled to benefit further from the success of the Project in case of "Excess Annual Revenues" and an increase in the value of the core assets of the infrastructure to be built during the 10-years duration of the contract signed.

VII.3. The distortions of competition and the effect on trade are limited, so that the overall impact of the measure is positive

- (73) The Commission concludes that the notified measure will contribute to offsetting the regional imbalances between the North West and other parts of the island of Ireland due to the existence of the border between Northern Ireland and the Republic of Ireland, and is objectively justified to address the lack of direct international connectivity in the region. In view of the characteristics of the project and of the safeguards applied by the UK authorities, the overall impact on competition is deemed to be positive. On the effect on trade, the Commission does not identify negative spillovers for other Member States.
- (74) On balance, the Commission concludes that the overall effect of the measure is deemed to be 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 (the provision of electronic communications services and networks, including the provision of international connectivity, and indirectly the provision of broadband services). The

intervention is designed in a way that does not distort competition or affect trading conditions to an extent contrary to the common interest.

VII.4. Conclusion

(75) 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.

VIII. DECISION

On the basis of the foregoing assessment, the Commission has accordingly decided that the aid measure "*Direct International Communications Links into the NW of Ireland* " is compatible with Article 87(3)(c) of the EC Treaty.

The UK authorities are reminded that, pursuant to Article 88(3) of the EC Treaty, they are obliged to inform the Commission of any plan to extend or amend the measure.

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

Your request should be sent by encrypted e-mail to stateaidgreffe@ec.europa.eu or, alternatively, by registered letter or fax to:

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Yours faithfully,

For the Commission

Neelie KROES
Member of the Commission