



Cable Europe

Cable Europe's response to the European Commission's Consultation on its draft Guidelines for the application of State Aid rules in relation to the rapid deployment of broadband networks

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The European cable TV industry currently provides broadband, telephony, digital TV to over 73 million customers. Cable Europe, the European Cable Communications Association, represents all leading European cable TV operators and their national trade associations. The aim of Cable Europe is to promote and defend the industry's public policy positions and business interests at both European and international level, and to foster co-operation among its members.

Cable Europe welcomes the opportunity to comment on the European Commission's draft Guidelines for the application of State Aid rules as they apply to the deployment of broadband networks. However, as these Guidelines also relate to the NGA Networks developments, Cable Europe would like to request to the Commission to streamline closely these Guidelines with the Draft NGA Recommendation and considers it is also necessary to link it to other initiatives such as the forthcoming European Broadband Strategy. It is indeed essential that consistency is applied across these instruments.

Public involvement in European broadband markets has increased significantly over the past few years. As has been noted by the Commission, recent public broadband initiatives have not only involved investments in rural areas, but also the deployment of networks in urban areas where private broadband infrastructures are in most cases already in place.

While public involvement can make an important contribution to the development of a knowledge-based European economy, it also runs the risk of distorting both the present and future competitive structure and investment signals, which can in turn interfere with the commercial incentives to deploy NGA networks. This would be the case if such public intervention involves the granting of State Aid. Accordingly, it is necessary to adopt clear-cut and predictable State Aid rules concerning broadband deployments using State money.

European cable operators are playing an important role in the fostering of a European broadband market based on sustainable infrastructure competition. Broadband investments made by cable operators not only benefit cable

customers directly, but also serve as catalysts for investments made by other telecommunications operators. By upgrading cable networks and providing customers with some of the first NGA networks across the European Union, cable operators have compelled fixed PSTN incumbents, as well as other market actors, to invest more rapidly in new fibre-based networks.

Seen from this perspective, Cable Europe takes the view that State Aid for broadband investments must not distort existing infrastructure competition, nor should it undermine the preconditions usually associated with the development of competition. Cable Europe supports the public funding for the development of networks in areas where, due to market failures, it exists a persistent lack of commercial initiative by any private infrastructure providers to invest in the building of new, or the upgrading of existing, infrastructure. However, in such cases, State Aids should be proportionate to the market failure they intend to correct. For example, instead of crowding out the private initiative by deploying a full network to the end customers from scratch, State Aid could take the form of funding a trunk network to towns with a lesser population density so that private investors could find profitable to deploy their access networks there. Cable companies might be willing to team up with public authorities to invest in these areas. This is why fair open tenders are the most essential element of the funding process, as they provide cable companies the possibility of participating on a level playing field in the tenders for such development projects.

In the Commission's draft Guidelines, it is stated that the Commission aims at "*increasing legal certainty and the transparency of its decision-making practice*". Cable Europe welcomes this objective and points out that the Guidelines, when finally approved, can play a key role in guiding public institutions in both their planning and implementation of broadband investments. As such, the Guidelines can constitute an important input into the business and investment plans of private broadband operators, including cable operators, and have a positive impact on both the speed and the character of NGA roll-out.

However, in order to be able to satisfy the dual objectives of legal certainty and transparency, the Commission's draft Guidelines require further elaboration in a number of key respects, including:

(a) *The grounds upon which the assessment of the compatibility of State Aid should be conducted.* Particularly the conformity of a public sector investment with the Market Economy Investor Principle should be demonstrated thoroughly and comprehensively.

(b) *Those areas in which public investment would be considered as being inherently compatible with State Aid rules.* In particular, the commercial realities underpinning private operators' market and business developments should serve as the benchmark for such working presumptions.

(c) *How and on what grounds State Aid measures should be justified,* especially regarding the fact that the lack of investment by the private sector

should not be considered as providing, of itself, the justification for public intervention.

(d) *The requirements that need to be satisfied by the publicly funded infrastructure in order for it to be compatible with State Aid rules, particularly the proportionality of the measures to the results sought and how the relevant wholesale access obligation should apply.*

Cable Europe proposes that further elaboration is required in relation to the issues outlined immediately below:

- **The assessment of the Market Economy Investor Principle (“MEIP”)** (Section 2.2.1, points 16-19)¹
 - The significant participation of private investors alongside a public body needs to be assessed under very strict grounds in determining their compatibility with State Aids rules. Moreover the provision of wholesale or retail broadband services by public bodies, either by themselves or alongside with private investors, needs to be assessed firstly from a market perspective in order to ascertain whether such provision is indistinguishable with that by a private undertaking absent state aids. Otherwise, as the draft Guidelines points out, the public intervention will constitute State Aid. To carry out that assessment the Commission applies the so called Market Economy Investor Principle test (MEIP test). In practical terms, the most important part of the MEIP assessment procedure should be the assessment of the public investor’s Business Plans. According to the draft Guidelines, the Business Plan should be sound and should show an adequate return on the investment. Cable Europe welcomes the fact that the draft Guidelines point out that the conformity of a public investment with commercial market terms should be *“demonstrated thoroughly and*

¹ According to the MEIP test, State Aid is not involved where an investment is made by the State in an undertaking on terms and conditions which would be acceptable to a private investor of a size comparable to that of bodies managing the public sector operating under normal market conditions. The principle applies to all public institutions, regardless of whether they are profit or loss making. Consequently, the standard used in the assessment of the MEIP test is that "State aid is not involved where an investment is made by the State in the undertaking on terms and conditions that would be acceptable to a private investor of a size comparable to that of bodies managing the public sector operating under normal market conditions." (See Case C-142/87 Belgium v. Commission [1990] ECR I-959, at para. 29.) Over the course of time, the principle has been expanded by the European Courts to include the principles of the “private creditor” and the “private buyer”. The yardstick for assessing the MEIP test is still found in a Commission Communication of 1984, although a number of additional comparators with private firms have been introduced in practice over the years, especially in those circumstances where the public undertaking is unique on the market and a comparison with a private investor would therefore be inappropriate.

comprehensively". This should be applicable to both public authorities and publicly owned city networks/ publicly owned housing companies. However, in order to facilitate the procedure and to increase the certainty of its outcome, the Commission needs to further clarify:

- *Lack of a Business Plan*: Although arguably implicit in the terms of the proposed Guidelines, it would be preferred if it were set out expressly in the Guidelines that the lack of a Business Plan at the time of the investment is, as such, a sufficient basis to conclude that the MEIP has not been satisfied. Accordingly, the public sector investment would be deemed to involve the grant of State Aid and should be assessed accordingly.
- *The burden of proof*: In the application of State Aid rules, it has always been problematic as to whether the complainant or the defendant should bear the burden of proving the soundness of the public authorities' Business Plan. Therefore, it would be very helpful if the Commission would clarify that the burden of proof in principle always rests upon the public body, and that the decision to implement a broadband investment by any public body must be based upon a well documented Business Plan that should also be easily accessible to the public.
- *Catalogue of requirements*: Another issue which arises in the application of the MEIP is the level of proof required to substantiate that the Business Plan is indeed sound and demonstrates that an adequate return on investment will be achieved (*i.e.*, the meaning of the phrase "*demonstrated thoroughly and comprehensively*"). To increase legal certainty in this regard, the Commission should define a set of minimum standard requirements, based on financial criteria, which must be satisfied by the public body in order to demonstrate that its Business Plan satisfies the MEIP standards. Further, the Guidelines should define a set of requirements for the safeguarding of such an assessment.

For example, the Guidelines would be more effective if they were to set out the financial indicators that should be used to analyse the soundness of the Business Plan. A requirement could also be added that any business plan presented as the basis for a public sector investment should be audited and accepted by a reputable independent audit company.

In addition, a requirement could be added that the public investor should establish a regulatory Impact Assessment in order to be able to substantiate the robustness of the Business Plan. Finally, a clause limiting the possibilities of the selling on of the publicly funded network should also be added to the Guidelines, as this could also have an impact on the overall amount invested. Indeed, the funds provided should not be a disguised means of providing funds to another private operator as this could impact adversely on the competitive balance in the area and therefore raises the question of whether the funds are actually required. If selling on is to be permitted, it should only be on non-discriminatory and transparent grounds. Any attempt of selling on a State-subsidised asset should in principle be subject to advance public notification and should be open to all interested operators.

- Calculating an adequate return on investment: An important aspect of the analysis of the State measure's compatibility with the MEIP is the assessment of the estimated return on investment. In several cases, it has been unclear on what basis the return on investment should be calculated, namely, whether the investment should be viewed as a broadband (in general, high risk) investment or as a real estate (in general, low risk) investment. The Commission's Guidelines should further clarify the principles to be applied when calculating a reference return on investment, against which the applied return on investment estimate could be benchmarked (in this respect, the Guidelines should arguably contain a reference to the forthcoming EC Recommendation on NGA regulatory principles - as they will address this question - and also to future NRA regulatory practice in the application of that Recommendation, as the final "risk premium" for broadband projects has yet to be set by NRAs).
- **The assessment of well-defined objectives of State Aid measures** (Section 2.3.2, points 32-38; Section 3.1 point 47; Section 3.3, points 60-65; Section 3.4, points 67-73)
 - The case of "white", "grey" and "black" areas: In deciding whether a proposed measure is compatible with State Aid rules, the Commission highlights the distinction between "white", "grey" and "black" areas. This distinction is applied, with certain modifications, to both "traditional" and "NGA scenarios".

Cable Europe applauds the Commission's principle established in the Guidelines (point 72) by which it considers that where two '*basic broadband providers*' are already competing to provide broadband services, no further State intervention should in principle be necessary in order to provide correct incentives to existing operators to invest. The burden of proof to reverse this principle (*i.e.*, that both operators do not plan to make investments) indeed lies on the Member State/local authority (-ies) proposing to fund a new broadband or NGA network.

Moreover, Cable Europe would suggest to include a new paragraph 72bis whereby the Guidelines clearly says that in order to assess if a given area where basic broadband is already present qualifies as a "black" NGA area the Commission will specially take into account the presence of cable networks that can be easily upgraded to NGA as such upgrading might be done through a lower investment and within a time period sensibly shorter than traditional incumbents' networks.

Likewise, in the assessment of whether a given area is grey or black, the Commission could set the principle that when there is likely to be at least one cable network upgraded to NGA in that area, there should also be an automatic presumption that the incumbent is likely to deploy its own fibre network, as historically the evidence suggests that one of the main drivers for incumbents' investment is precisely infrastructure competition provided by cable. The area should consequently be considered as a "black" NGA area.

However, since State Aid measures are often conducted by local public authorities and the measures often cover entire municipalities and cities, a common problem in practice occurs where a municipality or a city contains hybrid elements of each of the respective "white", "grey" and "black" categories (in other words, sub-areas or sub-regions).

If State Aid is granted to a "white" sub-area and the city network also covers a "black" sub-area, there exists a substantial risk that cross-subsidisation will take place between the State-aided parts of the network and those parts of the network which are supposed to be deployed on commercial conditions (the parts that cover the "black" sub-areas). Indeed, funds received for one part of the business should not be used to help to sustain a loss elsewhere. Therefore, in hybrid areas, the assessment should first and foremost consider the likelihood whether a white/grey area adjacent to a black area will evolve in the near future into a

black area itself, largely due to spillover effects. In these circumstances, a State-funded project that is considered to be truly hybrid should be only approved within the existing borders of the white/grey portion of the overall geographic area in question, and altogether prohibited in the black portion.

- *The greater specification of the term "in the near future"*: In translating the principles of "white", "grey" and "black" areas into the NGA scenario, the Commission uses the term "in the near future" and suggests that such a period should correspond to a period of five (5) years. The Commission's argument is that the 5 year period appears to correspond to the average period needed for the deployment of a Next Generation Access network covering a town or a city.

Cable Europe takes the view that the Commission's 5 years horizon and the arguments supporting that timeline are not wholly consistent with the commercial realities of a private operators' market and with business developments currently witnessed. The question should therefore not be how much time is required to deploy an NGA network in a town or city in terms of its technical feasibility, but rather whether – by taking into account factors such as population density, demand forecasts, etc. - it is likely that an operator will undertake an NGA deployment. That question is inextricably linked to the issue raised immediately above as regards the geographic segmentation of a municipality broadband project into sub-areas (some "white", some "grey", some "black") where the likelihood and timing of NGA network deployment by private investors would differ. For instance, in new urban developments within highly populated areas such as Madrid, London or Amsterdam, the fixed PSTN incumbent operator is probably prepared to deploy an NGA network within a period of less than 5 years. Likewise, in densely populated areas where cable has already deployed hybrid coaxial-fibre networks, a EuroDOCSIS 3.0 upgrade to an NGA network would take a relatively short time to be undertaken if demand conditions are satisfied. On the other hand, if the area considered is a whole city or municipality, a period of 5 and even 7 years would be more in accordance with both the technical and market realities currently being witnessed (even in the absence of the current economic recession).

- *Economics of density*: According to the Commission, one of the objectives of a State aid is to respond to a market failure arising from the lack of investment due to the economics of density. Cable Europe considers, however, that whereas economics of density represent clear barriers to entry, they

do not necessarily justify the per se duplication of networks as the appropriate policy response. The economics of density might indeed represent a market failure and may result in the existence of only one network, but the main concern from a public/economic policy perspective is the existence of a monopoly provider. The correct response to this situation, however, is not the inefficient duplication of a network so that there are two or more networks operating at an inefficient scale, but rather to either regulate the monopoly provider's retail prices or, preferably, impose regulated access to the monopoly provider's bottleneck assets (see further below).

- Defining NGA networks: As already stated above, the Commission suggests that State Aid could be used to support the rapid deployment of NGA networks. Cable Europe believes that any definition of the concept of "NGA" established under these Commission Guidelines should be consistent with that which will be set forth in the forthcoming NGA Recommendation. Cable Europe questions the need to further define an NGA network with different technological criteria (other than in the context of determining whether it should be subject/can be subject to an appropriate access obligation). In our view, setting speeds limits is not necessary for this purpose and runs the risk of being inaccurate, misleading or not sufficiently forward-looking with regard to the technology to be deployed. It is much more important to deploy a fiber network in the access network than concentrating on a certain bandwidth when technology improves so rapidly. Should this definition remains technology-specific, we urge the Commission to revise it as well as the whole Guidelines on an annual basis.

Moreover, as being a first step towards the FTTH network and providing similar services as the cable networks based on EuroDOCSIS 3.0 cable modem standard, any network built upon the VDSL or VDSL2 technology should also be expressly included in this definition.

- **Public authorities' analyses demonstrating the necessity of State aid measures** (Section 2.3.3, point 45 a; Section 3.4.4, point 73)
 - The risk of biased market analyses: In its description of the assessment of the proportional character of a notified measure in "white" and "grey" areas (both in the traditional and in the NGA scenario), the Commission highlights, among other conditions, that Member States/the relevant public

authorities should conduct market analyses before carrying through a State funded broadband project.

Cable Europe notices that, in the Commission's suggested procedure, the public authority that is presumably implementing a State Aid measure is also conducting the market analysis that is supposed to demonstrate the necessity of the same measure. It is inherent in such a procedure that the public authority involved has strong inducements to conduct a pessimistic analysis of likely future investment, thereby clearly justifying the need for its own involvement.

To minimize the risk of biased market analyses occurring, the Commission should first elaborate which requirements should apply to Member States'/public authorities' market analyses, and second reinforce this position by specifying in the Guidelines that the market analyses should be notified to and approved by the relevant national expert agencies, such as the relevant NRA and/or the NCA.

- Tracking historical patterns of investment: In the specific case of existing basic broadband "black" areas, as underscored above, the Commission establishes that State Aid should in principle not be necessary in such areas. Yet, the Commission notices that Member States/public authorities can rebut such an argument by demonstrating that the historical pattern of the investments made by network operators has not been satisfactory.

Again, Cable Europe highlights that the public authority conducting the analysis of historic investments has strong inducements to conduct a pessimistic analysis which clearly points to the need for its own involvement. Moreover, a number of factors relevant to such an analysis are unclear, including: the grounds upon which such an analysis should be conducted; the specific investment information required for the public authority to conduct its historical analysis; the relevant timeframe for analysis; and the method by which user satisfaction is to be estimated.

Even more importantly, the application of this principle presupposes that broadband deployment is a public good and that the State should take up the goal of deploying new networks if the private sector does not do so. Cable Europe does not consider this to be a sound working principle: a lack of investment by the private sector should not be in itself a justification for public intervention. For example, non-affordability at a given point in time should not *per se* be considered to constitute a market failure. It might be the

case that operators have not invested sufficiently because they do not perceive consumer demand in the short term for advanced services to be supported in NGA networks or because they have expectations of change in economic or regulatory conditions. However, markets can evolve quite rapidly and operators, being reactive to market conditions, might decide to invest at a given moment in time to be able to satisfy new demand or to take advantage of economic/regulatory conditions. However, public investment based on an alleged lack of interest by private parties might distort this process by substituting market-driven decisions for administrative ones.

In Cable Europe's view, the provision described above runs a high risk of leading to arbitrary evaluations of the worth of historic investments. Point 73 in the draft Guidelines should therefore be deleted.

- **The assessment of well-designed measures** (Section 2.3.2 point 40; 2.3.3, point 45 ff; Section 3.4.5, point 74)
 - Proportionality of the measure: The Commission is of the view that regulating an incumbent operator – particularly one in a grey/black area – might not be sufficient to provide affordable broadband services to users in that area, and that State Aid for the deployment of a parallel network is therefore necessary. Cable Europe questions the validity of this assumption in every case. Why would the deployment of an entirely parallel network with public funds (with imposed access) be more valuable from a consumer's perspective than just imposing access on the incumbent's network? It seems difficult to identify a situation where there is at least one network and the effective regulated access of the incumbent's network – be it in the form of access to ducts or wholesale bitstream access – is not sufficient to guarantee the provision of competitive broadband services to users. If the deployment of a second network is not economically attractive to an alternative operator, why should it be more valuable for consumers to have their government deploy an entirely new network which implies higher costs that are to be financed with consumers' taxes? Cable Europe therefore considers that access regulation on the incumbent's network should be the first option used to guarantee competition, and the failure of such competition to materialize will have to be assessed by NRAs in close cooperation with the Commission.
 - Defining wholesale access in the "traditional scenario": In assessing the proportional character of a measure in traditional "white" or "grey" areas, the Commission

establishes that third party access to a subsidized broadband infrastructure is a necessary component of any State measure. The Commission also suggests that wholesale access should be granted for at least a period of seven (7) years.

Cable Europe welcomes the Commission's views on the importance of wholesale access to subsidized infrastructure, but also notes that the draft Guidelines lack an explanation on the pricing principles to be applied with respect to such access. It is indeed essential that wholesale prices are set at an efficient level, so as to avoid the devaluation of past investments made by private operators, and in particular to avoid any creation of bias towards non facility-based new entrants *vis a vis* cable operators, as the latter have to compete with incumbents in spite of their much lower scale of operations without receiving the benefit of lower access prices.

- Defining wholesale access in the "NGA scenario": As regards the additional requirements required to be established in the NGA scenario, the Commission suggests that subsidised networks in grey NGA areas should be open to third parties at wholesale level for a period of at least seven (7) years. The Commission suggests that the access should include access, for example, to facilities such as ducts and street cabinets, and that State Aid measures should support multi-fibre architectures that can be unbundled.

Cable Europe welcomes the proposed requirements on wholesale access to subsidised infrastructures. Yet again, however, Cable Europe emphasizes that wholesale prices must be set at effective levels so as to not facilitate inefficient entry, devalue past investments and, in particular, not create a bias towards non-facility based new entrants *vis a vis* cable operators, as the latter need to compete with fixed incumbents in spite of their much lower scale of operations without receiving the benefit of a lower access price.

- Defining wholesale access in the specific NGA case of existing basic broadband "black" areas: For existing basic broadband "black" areas, the Commission suggests that the aid should not cover the 'last mile' access segment, which is defined as being the segment connecting the end user or business premises to the Main Distribution Frame (MDF).

Cable Europe notes that the Commission continues to define the last mile access segment in relation to a traditional copper line scenario. Given the relatively unique importance

that the Commission and public authorities attach to the roll-out of NGA networks, Cable Europe considers it unlikely that the networks being deployed with the assistance of State Aid would have the same architecture as a traditional copper-based network. The definition provided by the Commission in its draft document is therefore not future-proof, and any limits to the granting of State Aid should rather be applicable to different NGA scenarios such as FTTCabinet and FFTBuilding. Cable Europe considers that further clarification of the implications of these particular network configurations is likely to be necessary.

In closing, Cable Europe wishes to reiterate its general support for the views expressed by the Commission in its draft Guidelines. What is required, however, is that more details be provided in the interpretation of certain key elements of the Commission's analysis, and that additional checks and balances be instituted in such a way as to ensure that the public authorities of Member States do not have unfettered discretion in their crafting and implementation of State Aid schemes. In both instances, the concerns of Cable Europe lie in the fact that State action in furtherance of public welfare should only be permissible where the effects of that action do not distort the conditions of competition, and the signals for investment, in a liberalized electronic communications environment.
