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PROFESSOR A.A. DASHWOOD

OPINION

RE:

CERTAIN QUESTIONS CONCERNING THE IMPLICATIONS IN EU LAW OF THE POSSIBLE ADOPTION OF THE "BaK" CHARGING MODEL FOR VOICE CALL TERMINATING SERVICES

Introduction

1. I am instructed, on behalf of Tele2 AB, to advise on issues of European Union Law (***EU Law***) in the field of telecommunications that may arise, if the charging model for voice call terminating services at the wholesale level, known as "Calling Party Network Pays" (***CPNP***), which is currently used in the EU, were required to be replaced by the model known as "Bill and Keep" (***BaK***).

2. In my understanding, the essential difference between the two charging models is this. Under CPNP, the operator of a telecommunications network that originates a call destined to be received by a subscriber of a different network pays a "termination charge" to the operator of that network, as consideration for providing the wholesale service of interconnection. Under BaK, there are no payments between network operators for termination services; in other words, mandated BaK would entail "termination charges effectively set at zero." [1] According to the definition used by the European Regulators Group (***ERG***):

   "BaK is a wholesale billing regime under which each network bears the cost of terminating traffic coming from other carriers. Therefore, under BaK the terminating access network operator does not receive payments at the wholesale level for the termination provided. Instead, it recovers its net costs incurred for termination – and any payments for upstream connectivity – in other ways, e.g. by billing them to its end customers".[2]

3. The questions that I am asked to address specifically are the following:

   (1) Given the fact that there is indeed a cost incurred when an operator receives a call from another operator, does that cost have to be covered by the party asking for/buying the service or is it possible to take the view that it is

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[1] See the Ofcom discussion document, "Wholesale mobile voice call termination", published 20 May, hereinafter "the Ofcom document", at paragraph 1.14, sixth bullet.

[2] ERG Draft Common Position on Next Generation Networks Future Charging Mechanisms / Long Term Termination Issues, ERG (09) 34 (hereinafter, "the ERG Draft Common Position"), para. 3.1.

sufficient that the so-called terminating operator's costs are covered through his other services?

The question, it is suggested, is probably linked to the fact that the market has been defined as a market for call termination where the operator has been viewed to have significant market power (***SMP***) and as such will be subject to an obligation of cost orientation.

(2) Article 13 of Directive 2002/19/EC (***the Access Directive***) seems to give an operator who offers termination the right to a reasonable rate of return on adequate capital employed. Would it, against this background, be within the legal possibilities of a Member State to introduce mandated BaK as the new termination regime. Similarly could the European Commission amend its Recommendation in such a way as to recommend Member States to introduce BaK instead of the now recommended long run incremental cost (***LRIC***) model?

(3) What would the consequences be for a Member State that decides to introduce BaK in breach of the Access Directive?

(4) What legal possibilities would an operator have if a Member State decides to impose BaK, thus setting aside the Access Directive?

Background

4. As part of the new regulatory Framework (***NRF***) for electronic communications networks and services in the EU that was established in 2002,[3] Member States are required by Article 8 (1) of the Access Directive to ensure that their national regulatory authorities (***NRAs***)[4] are empowered to impose on network operators a series of obligations identified in Articles 9 to 13 of the Directive. Article 8 (2) provides that "[w]here an operator is designated as having significant market power on a specific market... [NRAs] shall impose the obligations...as appropriate". They may not impose those obligations on undertakings that have not been so designated.[5]

[3] This comprises a "Framework Directive", Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communications networks, OJ 2002 L 108/33, and three "Specific Directives". Of the latter, the "Access Directive", Directive 2002/19/EC of the European Parliament and of the Council of 7 March 2002 on access to, and interconnection of, electronic communications networks and associated facilities, OJ 2002 L 108/7, is more particularly relevant for the purposes of this Opinion. The legislation, including the Access Directive, was amended by Directive 2009/140/EC of the European Parliament and of the Council of 25 November 2009, OJ 2009 L 337/37. The deadline for the implementation of Directive 2009/140/EC is 25 May 2011.

[4] As provided for by the Framework Directive, Article 3.

[5] Access Directive, Article 8 (3).

5. The notion of "significant market power" is defined for the purposes of the NRF by Article 14 (2) of the Framework Directive in terms derived from familiar case law of the Court of Justice on the meaning of a "dominant position" in Article 102 TFEU (ex Article 82 EC).[6] Pursuant to Article 15 of the Framework Directive, the Commission was required to adopt a recommendation on relevant product and service markets and also to publish guidelines for market analysis and the assessment of significant market power, of which NRAs must take "the utmost account". In the light of the indications provided by the relevant Recommendation[7] and Guidelines,[8] I understand from my Instructions that NRAs throughout the EU have defined as relevant markets the respective market for voice call termination provided by each individual network operator; from which it follows that every operator possesses significant market power in respect of its own network and is, accordingly, liable to be subjected to the obligations identified in Articles 9 to 13 of the Access Directive.

6. Article 13 (1) of the Access Directive provides that NRAs may "impose obligations relating to cost recovery and price controls, including obligations for cost orientation of prices and obligations concerning cost accounting systems, for the provision of specific types of interconnection and/or access in situations where a market analysis indicates that a lack of effective competition means that the operator concerned might sustain prices at an excessively high level, or apply a price squeeze, to the detriment of end-users". This power of NRAs is qualified by the following sentence of the paragraph, which reads: "National regulatory authorities shall take into account the investment made by the operator and allow him a reasonable rate of return on adequate capital employed, taking into account the risks involved". The language of the qualification is further strengthened in the version of Article 13 (1) that will result from its amendment by Directive 2009/140/EC.[9]

7. I understand, once again from my Instructions, that the methodology widely adopted by NRAs in the EU for the purpose of ensuring cost orientation of termination charges is one based upon "long run incremental costs" (***LRIC***). Ofcom explains its LRIC methodology, in broad terms, as reflecting the additional costs of providing wholesale call termination, including a share of the fixed and common costs an operator is likely to incur in running a network that supports a number of services.[10] However, I have further been informed,

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[6] E.g. Case 322/81, *Michelin BV* v *Commission* [1983] ECR 3461, para.6.

[7] Commission Recommendation 2003/311/EC of 11 February 2003 on the relevant product and service markets within the electronic communications sectors susceptible to *ex ante* regulation in accordance with Directive 2002/21/EC, OJ 2003 L 114/45; revised by Recommendation 2007/879/EC of 17 December 2007, OJ 2007 L 344/65.

[8] Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services, OJ 2002 C 165/6.

[9] Discussed below, paragraph 34.

[10] Ofcom document, para. 1.6.

the LRIC methodology has been implemented by NRAs in divergent ways, with the practical result that the calculated cost for termination in different Member States has varied significantly.

8. Consistently with that view, the European Commission has noted that "[a]lthough some form of cost orientation is generally provided for in most Member States, a divergence between price control measures prevails across the Member States", which is explicable both by "a significant variety in the chosen costing tools" and also "different practices in implementing those tools".[11] In May 2009 the Commission, therefore, adopted a Recommendation on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU (***the Commission's termination rate Recommendation***), laying down criteria for setting rates related to the costs incurred by an efficient operator.[12] The evaluation of efficient cost, it is stated, should be "based on current cost and the use of a bottom-up modelling approach using long run incremental costs (LRIC) as the relevant cost methodology".[13] The Ofcom document describes the recommended approach as, broadly, amounting to a long run *marginal* cost methodology, since it makes no allowance for recovery of common costs.[14] At all events, it seems clear that implementation of the Commission's termination rate Recommendation would bring about a significant reduction in the rates, especially those applicable to mobile termination, from an average 8.5 eurocents in 2008 to a range of between 1.5 and 3 eurocents.[15] The deadline for compliance with the Recommendation has been set as 31 December 2012, with a possible extension in exceptional circumstances, more particularly on account of an NRA's limited resources, to 1 July 2014.

9. The approach of the Commission's termination rate Recommendation remains faithful to the established CPNP charging model, while seeking to harmonise the cost-recovery methodology employed by NRAs. Consideration was given to alternative models, including BaK,[16] the Commission noting that there is no record of BaK being imposed by a regulatory authority: "it generally results from *voluntary* agreement between interested parties, which in certain circumstances choose to set these fees at zero, particularly where the net financial settlements are equal to or close to zero".[17] After briefly reviewing some of the pros and cons of BaK, the Commission concludes: "a

[11] Commission Recommendation (2009/396/EC) of 7 May 2009 on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU, OJ 2009 L124/67, recital (2).
[12] *Ibid.*, point 1.
[13] *Ibid.*, point 2.
[14] Ofcom consultation document, para. 1.14, third bullet.
[15] Commission Staff Working Document accompanying the Commission Recommendation on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU, *Implications for Industry, Competition and Consumers*, SEC (2009) 599., para. 4.2.1.
[16] Commission Staff Working Document accompanying the Commission Recommendation on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU, *Explanatory Note*, SEC (2009) 600, para.6.1.
[17] *Ibid.*, para.6.1.2. Emphasis added.

significant reduction of termination rates might create appropriate incentives for voluntary inter-operator agreements and consequently Bill and Keep type arrangements could evolve naturally".[18]

10. The concerns expressed in the questions that have been put to me were aroused by the ERG Draft Common Position, which went out to consultation in October 2009. This canvasses the possibility of a future alteration of termination charging models, from CPNP to mandated BaK. After a lengthy review of a variety of technological and economic considerations, the ERG Draft reaches the tentative conclusion that "BaK is more promising than CPNP as a regulatory regime for termination for the long term and based on national circumstances (including legal issues) NRAs could set a glide path to BaK within the regulatory period related to the next market analysis they carry out for voice termination".[19] No further indication is given as to the nature of the "legal issues" there referred to; nor are such issues examined elsewhere in the ERG Draft,[20] nor indeed in the discussion of BaK in the Commission's termination rate Recommendation. On the other hand, the Oftel consultation document recalls that "Article 13 of the Access Directive imposes requirements on NRAs when setting charge controls as SMP conditions, and goes on: "If necessary, we will need to consider how alternative remedies (for example 'bill and keep') might meet [those] requirements...".[21] It seems, therefore, that Tele2 is not alone in having doubts about the compatibility of BaK with the EU regulatory Framework.

The First Question

11. The first question invites me to consider whether, given the fact that there is indeed a cost incurred when an operator receives a call from another operator, that cost has to be covered by the party asking for/buying the service or whether it is possible to take the view that it is sufficient that the so-called terminating operator's costs are covered through his other services. The question, my Instructions suggest, is probably linked to the fact that the market has been defined as a market for call termination where the operator has been viewed to have SMP and as such will be subject to an obligation of cost orientation.

12. As I have noted above,[22] mandated BaK would mean that termination charges were effectively set at zero. In other words, not only would the terminating operator be unable fully to cover the actual costs of receiving the call: he would be prohibited from imposing any charge at all.

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[18] *Ibid.*
[19] At p. 55, *in fine.*
[20] As noted in Tele2's Response to the ERG Consultation, at p.37.
[21] At point 6.8, p.31.
[22] Paragraph 2 and footnote 2.

13. The intention of the Union legislator to achieve complete harmonisation of the obligations that can be imposed on network operators having significant market power is evident from the second subparagraph of Article 8 (3) of the Access Directive.[23] This provides:

"In exceptional circumstances, when a [NRA] intends to impose on operators with significant market power other obligations for access or interconnection than those set out in Articles 9 to 13 in this Directive it shall submit this request to the Commission. The Commission...shall take a decision authorising or preventing the [NGA] from taking such measures".

NRAs may not, therefore, be given autonomous power, outwith the NRF, to impose obligations regarding access or interconnection upon operators having significant market power; they may act only when authorised pursuant to Articles 9 to 13 of the Access Directive or, in exceptional circumstances, with the specific agreement of the Commission.

14. In my opinion, it would not be open to the Commission to use this exceptional power, which is clearly intended to be exercised on a case-by-case basis, in order to authorise NRAs to prescribe BaK as the standard charging (or, rather, non-charging) model for terminating services. It follows that mandated BaK could only be imposed in substitution for CPNP, whether on the initiative of NRAs or in response to a Commission recommendation, if such a change were found to be within the scope of the authorisation conferred by Article 13 (1).

15. In accordance with settled case law, the provisions of the Access Directive, like those of any other act of the Union's institutions or of the Treaties themselves, fall to be interpreted in the light of their wording, as well as their purpose and legal context.[24] With no guidance from the Court of Justice that is directly on the point, it is impossible to say with complete certainty that the imposition of a BaK regime, preventing the actual cost of interconnection from being covered by a charge levied by the terminating operator on the originating operator, would not be within the scope of the power exercisable by NGAs pursuant to Article 13 of the Directive. Nevertheless, it appears to me that a strong case can be made to that effect, having regard both to the express terms of Article 13 and to its function within the general system of the Access Directive and of the Framework Directive, as a corrective tool fashioned to deal with a specific

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[23] To the same affect, see P. Nihoul and P. Rodford, *EU Electronic Communications Law* (hereinafter, *Nihoul*) para. 3.117, p. 220; I. Walden (ed.), *Telecommunications Law and Regulation*, para. 7.4.2.4.3, p.333.

[24] For a recent authority in the field of telecommunications, see Case C-55/06, *Arcor AG & Co. KG* v *Germany*, judgment of 24 April 2008, paragraph 57.

instance of market failure. In addressing these matters, I shall not give particular attention to the second sentence of Article 13 (1), concerning the requirement for NRAs to take account of the investment made by the operator and to allow him a reasonable rate of return on capital, since I understand that to be the subject of the second question.

16. There are several elements in Article 13 that allow an argument to be developed based upon the letter of the text. It is stated in paragraph (1) that NRAs "may in accordance with the provisions of Article 8, impose obligations relating to cost recovery and price controls, including obligations for cost orientation of prices and obligations concerning cost accounting systems, for the provision of specific types of interconnection and/or access...". The former set of obligations might well have been assumed to comprehend the latter, but the Union legislator evidently thought it essential that the scope of the authorised powers be precisely defined. That would militate against an extensive interpretation of the same wording, such as to allow the complete prohibition of charging for termination services. Similarly, paragraph (2) requires NRAs to make sure that "any cost recovery mechanism or pricing methodology that is mandated" serves specified objectives, and goes on to mention that they "may also take account of prices available in comparable national markets"; while paragraph (3), on the transparency of cost accounting systems, notes that NRAs "may require an operator to provide full justification for its prices, and may, where appropriate, require prices to be adjusted"; and paragraph (4) focuses on the transparency of any mandated cost accounting system. Nowhere among those provisions, which are designed to elucidate the obligation referred to in paragraph (1), is there the least suggestion that a complete ban on charging was within the contemplation of the legislator. Considered as a whole, the text of Article 13 would seem to be predicated on the continuing existence of charges for interconnection and/or access, which may call for some form of control measure on the setting of prices.

17. Indeed, the provisions of Article 13 of the Access Directive are cited in a leading commentary on the EU's telecommunications legislation as a good illustration of the attempt made under the NRF to limit the obligations that may be imposed on undertakings having significant market power.[25] This is said to reflect "a concern that over-regulation should be avoided and that parties should be left free to develop their behaviour autonomously to the greatest extent possible".[26]

18. I do not believe it could seriously be contended that mandating BaK would infringe the terminating operator's fundamental right to the use and enjoyment of his property, or his right freely to pursue trade or professional activities, especially if there are ways of

[25] *Nihoul*, paras.3.51 and 3.52, p.194.

recouping termination costs otherwise than by a charge imposed on the originating operator. Nevertheless, the fact that such rights are recognised by EU Law,[27] and that any exercise of the powers conferred upon NRAs pursuant to Article 13 is liable substantially to impinge upon an operator's enjoyment of them, might be thought to provide a further reason for interpreting the Article restrictively.

19. Turning to the purpose of Article 13, understood in the wider context of the NRF, I note that the "philosophy" underlying the reform in 2002 has been said to be that "markets should be left free in situations where they can produce satisfactory outcomes".[28] The corollary, indicated by recital (25) of the preamble to the Framework Directive, is that *ex ante* regulation must serve the specific need of ensuring the development of a competitive market. The limited function of regulation in the harmonised system of the NRF is further emphasised by recital (27), which declares: "It is essential that *ex ante* regulatory obligations should only be imposed where there is not effective competition, i.e. in markets where there are one or more undertakings with significant market power, and where national and Community competition law remedies are not sufficient to address the problem". This policy commitment to a free, competitive telecommunications market, with regulation restricted to the control of significant market power, is echoed in several recitals of the preamble to the Access Directive, notably: recital (12), which acknowledges that obligations imposed under the previous regime should initially be carried over into the NRF, while calling for a review of those obligations "in the light of prevailing market conditions"; recital (13), which says that such a review "should be carried out using an economic market analysis based on competition law methodology", the aim being "to reduce *ex ante* sector specific rules progressively as competition in the market develops"; and Article (14), which says that the range of possible obligations that could be imposed, pursuant to Directive 97/33/EC,[29] on undertakings with significant market power (including price control)

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[26] *Ibid.*

[27] See, e.g., Case 44/79, *Hauer* [1979] ECR 3727, paras. 13 to 33. Such rights have to be weighed against the public interest objectives that may justify restricting them. The Charter of Fundamental Rights of the European Union contains an Article 17 protecting "the right to own, use, dispose of and bequeath...lawfully acquired possessions", which is modelled on Article 1 of the First Protocol to the European Convention for the Protection of Human Rights and Fundamental Freedoms.

[28] *Nihoul*, para. 3.72, p. 203. The judgment of the Court of Justice of 12 November 2009 in Case C-192/08, *TeliaSonera Finland Oij* appears to confirm that such a "philosophy" permeates the Access Directive. Citing recital (5) of the preamble to the Directive, and its Article 3 (1), the Court declares that "freedom for undertakings to negotiate and conclude agreements...forms part of the objective of the Access Directive" (paragraph 39); from which it is said to follow that an obligation, such as that provided for by Article 4(1), when the operator of a public communications network has been requested by an authorised undertaking to negotiate interconnection, "is an exception and must therefore be interpreted strictly". Similar reasoning, it is submitted, could be applied to the obligations that may be imposed by NRAs pursuant to Articles 9 to 13 of the Directive (paragraph 40).

[29] Directive 97/33/EC of the European Parliament and of the Council of 30 June 1997 on interconnection in telecommunications with regard to ensuring universal services and interoperability through application of the principles of Open Network Provision (ONP), OJ 1997 L 199/32.

"should be maintained but, in addition, they should be established as a set of *maximum* obligations that can be applied to undertakings, in order to avoid over-regulation".[30] The concrete expression of that policy commitment is found in Article 8 (2) and (3) of the Access Directive, where it is provided that the obligations set out in Articles 9 to 13 are to be imposed on operators designated as having significant market power and not upon other operators.

20. Consistently with the purpose of *ex ante* regulation in the system of the NRF, power to impose obligations relating to cost recovery and price controls is provided for by Article 13 (1) of the Access Directive "in situations where a market analysis indicates that a lack of effective competition means that the operator concerned might sustain prices at an excessively high level, or apply a price squeeze, to the detriment of end-users". Cost recovery and price control obligations are, therefore, authorised as a remedy for market failure, in order to avoid two kinds of undesirable outcome: that an operator enjoying significant market power might impose charges that are excessively high; or that, while seemingly charging reasonable wholesale rates for interconnection and/or access, such an operator may apply a "price squeeze" on competitors by reducing his prices for downstream services.

21. The particular obligations that an NRA imposes under powers derived from Article 13 of the Access Directive must, pursuant to Article 8 (4) of the Directive, "be based on the nature of the problem identified, proportionate and justified in the light of the objectives laid down in Article 8 of the [Framework Directive]"; those objectives (to be pursued by "all reasonable measures" that are proportionate to them) relate to the promotion of competition, the development of the internal market and the promotion of the interests of the citizens of the EU.

22. Any measure taken against an operator pursuant to Article 13 has to be justified on the ground that he would be in a position to exploit the significant market power resulting from control of his own network (designated in the ERG Draft, "the termination bottleneck")[31] by charging for the provision of termination services at rates that were excessive in themselves or liable to disadvantage competitors by way of a price squeeze, with detrimental effects for consumers. The measure must be based upon the nature of that particular problem, proportionate and capable of being judged reasonable as a way of pursuing the objectives in Article 8 of the Framework Directive. The issue is whether the introduction of mandated BaK would constitute such a measure.

[30] Emphasis added.

[31] ERG Draft, para.5.1.1, p.26.

23. The thrust of the case made in the ERG Draft is that, all things considered, BaK is the model best adapted to the development of Europe's telecommunications sector in the long term, owing to the expected convergence of separate networks "towards a multi-service (including voice) NGN IP-network".[32] If that were true (and Tele2's Response puts forward a number of reasons showing why it may not be), the proposed change might perhaps be regarded as compatible with the broad objectives in Article 8 of the Framework Directive; however, the objective of facilitating the convergence referred to in the ERG Draft ranges far wider than that of preventing the exploitation of dominance on the market for termination services through excessive pricing, which is the particular problem the powers conferred by Article 13 of the Access Directive must be used to address.[33]

24. The ERG Draft may, though, provide an answer to that argument, namely that, whatever ulterior advantages might result from its introduction, BaK would provide a particularly effective solution to the competition problems associated with the termination bottleneck. As the Draft claims:

"Although in principle the bottleneck is not eliminated in a BaK regime, the main competition problem, excessive pricing of termination rates, cannot occur anymore. So Bak eliminates excessive pricing and all detrimental effects that arise from them (sic), without the need of calculating and setting a cost-oriented tariff".[34]

25. It could, therefore, be argued not wholly implausibly that mandatory BaK may be regarded as an obligation "based on the nature of the problem identified" with respect to termination charging. On the other hand, it appears to me that a solution that involves prohibiting a network operator from charging anything at all for termination services, thereby compelling him to find other ways of covering the real costs of providing such services (let alone making any contribution towards a return on his investment), would be likely to fall foul of the principle of proportionality. I say only "likely", because lack of proportionality is a ground of challenge in EU Law that is frequently plea ded but seldom successful.

[32] *Ibid.*, Executive Summary, p. 4.

[33] Another justification put forward for the introduction of BaK in the ERG Draft is that account would be taken of the utility of a call to the recipient as well as to the caller (see the discussion under point 5.2 of the Draft). While acknowledging the uncertainty of cost and utility distribution, the authors of the Draft claim that "BaK is likely to internalize call and network externalities better than CPNP" (point 5.2.1.1, *in fine*). That argument, based on the allegedly greater economic rationality of BaK, might or might not carry weight, if the amendment of the existing legislative framework were being considered. It cannot, in my view, have any bearing on the interpretation of a provision like Article 13, which is specifically and only designed to serve as a means of preventing a particular form of abuse on markets where the discipline of effective competition is lacking.

[34] *Ibid.*, para. 5.1.1, p.27.

26. A classic formulation of the principle is to be found in the judgment of the Court of Justice in the *National Farmers' Union* case:

"...the principle of proportionality, which is one of the general principles of Community law, requires that measures adopted by Community institutions do not exceed the limits of what is appropriate and necessary in order to attain the objective legitimately pursued by the legislation in question; where there is a choice between several appropriate measures recourse must be had to the least onerous, and the disadvantages caused must not be disproportionate to the aims pursued".[35]

It is worth recalling that, as a general principle of EU Law, and one that has, moreover, been explicitly enshrined in Article 8 (1) of the Framework Directive and Article 8 (4) of the Access Directive, proportionality is a standard that has to be complied with not only by the institutions of the Union but also by the Member States when implementing Union acts.[36]

27. I consider there would a good chance of establishing that, since its introduction would clearly be more onerous for the operator concerned than the alternative remedy of imposing cost-related price controls, mandated BaK would constitute a measure disproportionate to the aims pursued by Article 13. The ERG Draft argues that BaK would significantly reduce regulatory costs and the uncertainty involved in determining regulated prices.[37] However, in my view, such considerations should not be seen as outweighing the disadvantage of BaK to the operator, given that there are detailed provisions on cost orientation of prices in Article 13, indicating that the Union legislator must have regarded this as a viable, indeed the normal and preferred, remedy for the perceived problem of market failure in respect of pricing.

28. Finally on the first question, I draw comfort from recital 20 of the preamble to the Access Directive, which is in these terms:

"Price control may be necessary when market analysis in a particular market reveals inefficient competition. The regulatory intervention may be relatively light, such as an obligation that prices for carrier selection are reasonable as laid down in Directive 97/33/EC, or much heavier such as an obligation that prices are cost oriented to provide full justification for those prices where competition is not sufficiently strong to prevent excessive pricing".

[35] Case C-157/96 [1998] ECR I-2211, para. 60.
[36] Case C-239/02 *Douwe Egberts* [2004] ECR I-7007.
[37] ERG Draft, para. 5.1.3, pp. 29 to 30.

The recital tends to confirm my interpretation of the letter of Article 13 by identifying price control as the appropriate remedy where market conditions entail the risk of excessive pricing. It also tends to confirm that recourse to BaK would be a disproportionate remedy, since an obligation that prices be cost oriented is identified as already constituting a relatively heavy form of regulatory intervention.

29. In the result, my answer to the first question is in three parts:

NRAs could not be empowered to impose a BaK regime in substitution for CPNP, unless this fell within the scope of the authorisation provided for by Article 13 of the Access Directive.

It is impossible to interpret Article 13 with complete certainty in the absence of guidance from the Court of Justice that is directly on the point. Nevertheless, there are strong indications to be drawn from the express provisions of the Article (even without consideration of the second sentence of paragraph (1)) that the substitution of mandated BaK for CPNP, with the consequence of preventing the actual cost of interconnection from being covered by a charge levied by the terminating operator on the originating operator, would not be within the scope of the powers that may (and must) be conferred upon NRAs pursuant to that Article.

Consideration of the function of Article 13 within the general system of the Access Directive and of the Framework Directive, as a corrective tool fashioned to deal with a specific instance of market failure, would tend to confirm those indications. This is more particularly so, because, even if mandated BaK could be regarded as an obligation based on the nature of the problem of lack of competition on the market for voice call termination, its imposition would be disproportionate to the aims pursued, which can perfectly well be realised by the less drastic measure of cost-oriented price controls.

The Second Question

30. After noting that Article 13 of the Access Directive appears to give an operator who offers termination the right to a reasonable rate of return on adequate capital employed, the second question asks whether it would be within the legal possibilities of a Member State to introduce mandated BaK as the new termination regime; and similarly whether it would be open to the Commission formally to recommend the introduction of BaK in place of the presently recommended LRIC model.

31. The second sentence of Article 13 (1) is worded as follows:

*"[NRAs] **shall** take into account the investment made by the operator, and **allow** him a reasonable rate of return on adequate capital employed, taking into account the risks involved"*.[38]

32. The language of the provision is mandatory. In exercising the power of regulatory intervention that is authorised by Article 13, NRAs are legally required to take the investment made by the operator into account and, in addition, to allow him a reasonable rate of return on his capital. I cannot see how it would be possible for an NRA to comply with that duty under a regime where rates that could be charged for the service provided were compulsorily set at zero. The phrase "shall...allow him a reasonable rate of return" implies that price control measures imposed by NRAs must themselves be designed to secure network operators a reasonable return on their investment, and that it would not be sufficient for an authority simply to have satisfied itself that this could be obtained by other means such as payment for the services provided to consumers.[39]

33. Once again, recital (20) is supportive. It states:

"When a [NRA] calculates costs incurred in establishing a service mandated under this Directive, it is appropriate to allow a reasonable return on the capital employed, including appropriate labour and building costs, with the value of capital adjusted where necessary to reflect the current valuation of assets and efficiency of operations".

This more detailed explanation of how the allowance should be determined seems inconsistent with freedom for NRAs to prohibit charging completely.

34. The relevant sentence of Article 13 has been strengthened in the version of the Article as amended by Directive 2009/140,[40] through the addition of this introductory phrase:

"To encourage investments by the operator, including in next generation networks...".

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[38] Emphasis added.

[39] One of the issues in Case C-55/06, *Arcor*, footnote 24, above, was the interpretation of the phrase "cost-orientation" in Article 3 (3) of Regulation (EC) 2887/2000 of the European Parliament and of the Council of 18 December 2000 on unbundled access to the local loop, OJ 2000 L 336/4. The Court of Justice said that, as the principle governing the setting of rates for unbundled access to the local loop, cost orientation was to be understood as "the obligation on notified operators...to set those rates in accordance with the costs incurred in putting in place the local loop, while receiving a reasonable return from the setting of those rates in order to ensure the long-term development and upgrade of existing telecommunications infrastructures" (paragraph 69). While that interpretation was arrived at in the specific context of Regulation 2887/2000, it would be surprising if the identical phrase in Article 13 (1) of the Access Directive were found to have a wholly different meaning.

[40] See footnote 3, above. The amendment of Article 13 of the Access Directive is found in Article 2, point 9) of Directive 2009/140.

To the same effect, it is provided *in fine* that, in calculating a reasonable rate of return for the operator, account must be taken of "*any risks specific to a new network project*".

Those amendments are evidently designed to emphasise that future investments must not be deterred by over-zealous price-regulation.[41] This would apply *a fortiori* to zero rating of terminating charges.

35. I have already noted[42] that the power of the Commission, pursuant to Article 8 (3), second subparagraph, to authorise the imposition on operators with significant market power of obligations for access or interconnection other than those set out in Articles 9 to 13, is exercisable only in exceptional circumstances; so it could not be used to authorise the introduction of mandated BaK as the standard model for termination charging.

35. My answer to the second question is, therefore, that prescribing mandated BaK as the new termination regime would be incompatible with the legal duty upon NRAs, when exercising the power to impose obligations relating to cost recovery and price controls pursuant to Article 13 of the Access Directive, to allow operators a reasonable rate of return on their investment. Accordingly, it would not be within the legal possibilities of a Member State to adopt such a measure; and were the Commission to amend its termination rate Recommendation so as recommend the replacement of the LRIC model with BaK, it would be acting *ultra vires*.

The Third Question

37. The third question asks what the consequences would be for a Member State that decides to introduce BaK in breach of the Access Directive.

38. As I have noted in paragraph 13, above, it follows from the second subparagraph of Article 8 (3) of the Access Directive that the Union legislator intended the obligations that NRAs may be authorised to impose upon network operators to be confined to those set out in Articles 9 to 13 of the Directive. Therefore, if my interpretation of Article 13 is right, any Member State that introduced mandated BaK would be in breach of its obligations under the Treaties.

39. The relevant national legislation would not be null and void *ab initio*.[43] However, the courts of the Member State concerned would be bound, as a matter of EU Law, to

[41] Confirmed by recital 57 of the preamble to Directive 2009/140.
[42] Para. 14, above
[43] Joined Cases C-10 to C-22/97, *Ministero delle Finanze* v *IN-CO-GE*, [1998] ECR I-6307.

refrain from applying it, at all events in legal proceedings between the NRA and individual operators.[44]

40. The Member State would be liable to have infringement proceedings brought against it under Article 258 TFEU (ex Article 226 EC) by the Commission or (a remote possibility) under Article 259 TFEU (ex Article 227 EC) by one of the other Member States. The legal recourse available to the affected operators is the subject of the fourth question.

41. My answer to the third question is, therefore, that a Member State that decided to introduce mandated BaK in breach of the Access Directive would infringe its obligations under the EU Treaties, and all the usual legal consequences would follow.

The Fourth Question

42. The fourth question asks what legal possibilities an operator would have, if a Member State decided to impose BaK, thus setting aside the Access Directive.

43. The best course for an operator, in my opinion, would be to bring proceedings in the appropriate Member State court for judicial review of the national measure imposing mandated BaK. That assumes such a remedy to be available under the national legal system, and that the operator would satisfy the conditions for the admissibility of an action (which seems likely, in principle). The ground for contesting the validity of the measure would be its incompatibility with the Access Directive. If the national court had any doubts in the matter, it should be invited to make a reference for a preliminary ruling to the Court of Justice under Article 267 TFEU (ex Article 234 EC). Pending the ruling by the Court of Justice, the operator could apply to the national court for interim measures, which ought in principle to be available, but would only have to be granted if he could show that there were a risk of his suffering irreparable harm from the inability to impose wholesale termination charges (which seems unlikely, in practice).[45]

44. There would two other possible courses for the operator, neither of which I should advise.

45. The first would be to ignore the national measure and continue levying termination charges at the previously applicable rate, relying upon the direct effect of the Access Directive as a shield. It is trite law that, while natural or legal persons may not directly invoke the provisions of a directive in legal proceedings against another individual (a "horizontal" dispute), they may do so in proceedings against the national authorities of

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[44] Case 106/77, *Simmenthal* [1978] ECR 629. On the possibility for natural or legal persons to invoke provisions contained in directive in proceedings before a national court, see my answer to the fourth question.

[45] See Case C-213/89, *Factortame (No. 1)* [1990] ECR I-2433.

a Member State in default of its obligations under the directive (a "vertical" dispute).[46] However, reliance on the Access Directive for protection against any enforcement measure that might be taken by the NRA would be a risky option, since it cannot be guaranteed that the national court would accept the interpretation of the relevant provisions of the Directive that are proposed in my answers to the first and second questions, nor that it would be willing to make a reference to the Court of Justice; so the upshot for the operator might be exposure to a substantial penalty and perhaps a loss of reputation. There would also be a strong possibility that wholesale customers of the operator concerned would contest the legality of the charge in horizontal proceedings, where the provisions of the Directive could not be directly invoked (though it has to be conceded that the law on the so-called no horizontal direct effect rule for directives remains in a state of considerable uncertainty).[47]

46. The other possible option for affected operators would be a State liability action.[48] However, this would involve demonstrating that the impugned national legislation constituted a "sufficiently serious breach of EU Law", which might not be easy, given that there is some room for discussion about the scope of the power to impose obligations that is authorised by Article 13 of the Access Directive.[49] There could also be difficulty in establishing that the breach caused the operator financial loss, if it were possible for costs to be recouped and a return on capital secured in other ways.

47. In the result, my answer to the fourth question is that the best legal remedy available to an operator affected by a Member State's introduction of mandated BaK would be to seek judicial review of the relevant national legislation before the appropriate Member State court, and to invite that court to refer the question of the compatibility of the legislation with the Access Directive to the Court of Justice.

Summary of Advice

48. My answers to the questions that have been put to me are as follows:

(1) NRAs could not be empowered to impose a BaK regime in substitution for CPNP, unless this fell within the scope of the authorisation provided for by Article 13 of the Access Directive.

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[46] Case 148/78, *Ratti* [1979] ECR 1629; Case152/84, *Marshall (No. 1)* [1986] ECR 723; Case C-91/92, *Faccini Dori v Recreb* [1994] ECR I-3325.

[47] See my survey and analysis of the relevant case law, "From *Van Duyn* to *Mangold* via *Marshall*: Reducing Direct Effect to Absurdity?", (2006/2007) 9 *Cambridge Yearbook of European Legal Studies*, p.81.

[48] Case C-6/90, *Francovich* [1991] ECR I-5357; Joined Cases, C-46 and C-48/93, *Brasserie du Pecheur (Factortame no. 4)* [1996] ECR I-1029.

[49] See, e.g. Case 392/93, *BT* [1996] I-1631.

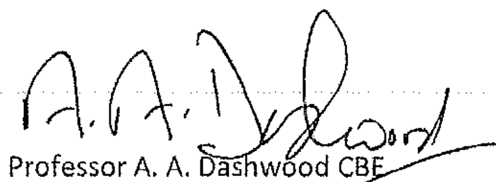
It is impossible to interpret Article 13 with complete certainty in the absence of guidance from the Court of Justice in a case that is directly on the point. Nevertheless, there are strong indications to be drawn from the express provisions of the Article (even without consideration of the second sentence of its paragraph (1)) that the substitution of mandated BaK for CPNP, with the consequence of preventing the actual cost of interconnection from being covered by a charge levied by the terminating operator on the originating operator, would not be within the scope of the powers that may (and must) be conferred upon NRAs pursuant to that Article.

Consideration of the function of Article 13 within the general system of the Access Directive and of the Framework Directive, as a corrective tool fashioned to deal with a specific instance of market failure, would tend to confirm those indications. This is more particularly so, because, even if mandated BaK could be regarded as an obligation based on the nature of the problem of lack of competition on the market for voice call termination, its imposition would be disproportionate to the aims pursued, which can perfectly well be realised by the less drastic measure of cost-oriented price controls.

(2) Prescribing mandated BaK as the new termination regime would be incompatible with the legal duty upon NRAs, when exercising the power to impose obligations relating to cost recovery and price controls pursuant to Article 13 of the Access Directive, to allow operators a reasonable rate of return on their investment. Accordingly, it would not be within the legal possibilities of a Member State to adopt such a measure; and were the Commission to amend its termination rate Recommendation so as recommend the replacement of the LRIC model with BaK, it would be acting *ultra vires*.

(3) A Member State that decided to introduce mandated BaK in breach of the Access Directive would infringe its obligations under the EU Treaties, and all the usual legal consequences would follow.

(4) The best legal remedy available to an operator affected by a Member State's introduction of mandated BaK would be to seek judicial review of the relevant national legislation before the appropriate Member State court, and to invite that court to refer the question of the compatibility of the legislation with the Access Directive to the Court of Justice.



Professor A. A. Dashwood CBE
Henderson Chambers
26 February 2010

OPINION

RE:

CERTAIN QUESTIONS CONCERNING THE IMPLICATIONS IN EU LAW OF THE POSSIBLE ADOPTION OF THE "BaK" CHARGING MODEL FOR VOICE CALL TERMINATING SERVICES

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