

Operational Separation as a means of preventing the abuse of Dominance on Access Markets

Cathal Flynn *

Introduction:

The leverage of dominance from one market onto another poses a threat to fair competition. This is especially the case in telecommunications, where market operators are vertically integrated, and where possession of essential network and infrastructure is usually in the hands of former state owned incumbents.¹ To realise such leverage of dominance onto downstream service markets, incumbent operators may frustrate, or limit, competitor's access to essential network and infrastructure. Whilst the current 2002 EU Regulatory Framework for Electronic Communications (the EU Regulatory Framework) addresses the issue of fair and reasonable access to bottleneck monopoly by means of the application of *ex-ante* market remedies, this approach is not fully satisfactory. There is no guarantee that the *ex-ante* obligations which ensure fair and reasonable access will be respected by the infrastructure owner, or that the infrastructure owner will not discriminate against competitors when offering terms of access. The concurrent application of *ex-post* competition law principles (Art. 82 EC Treaty) has also proven to be ineffective in deterring operators in possession of essential network and facilities at the bottleneck from abusing their position of dominance on access markets. This paper treats the current problems related to the enforcement of fair and reasonable access under the current EU

* Graduate of Law and European Studies (LL.B.) at the University of Limerick. Graduate of Masters in European Law (LL.M) at University College Dublin. Graduate of Masters in European Advanced Interdisciplinary Studies, College of Europe (M.A.) The author currently works in the Telecommunications Law Department of the Polish Law firm: Grynhoff, Woźny I Wspólnicy Sp.k.

¹ It is generally accepted that a vertically integrated operator, through its possession of essential network and infrastructure, has a powerful advantage at wholesale level that confers the ability to leverage its dominance onto downstream retail markets. These advantages include: bottleneck control of the local loop; vertical integration allowing the leverage of monopoly in some areas to support other areas; opportunity for "*cross-market*" leverage from strength in traditional markets into adjacent markets; network effects where customers benefit from being connected to larger networks; historical "*first-mover*" advantages; economies of scale; high economies of density; sunk costs (which allow the incumbent the scope to restrict entry by cutting prices to very low avoidable costs).

Regulatory Framework, and discusses the merits of applying a “*structural remedy*” onto the telecommunications market to address access related problems.

The current problem with the application of ex-ante remedies on the access market:

Theoretically, the EU Regulatory Framework ensures fair and reasonable access to facilities and infrastructure through the imposition of *ex-ante* obligations on market operators which have control of essential infrastructure, and which are found to have significant market power (SMP).² Such *ex-ante* obligations function in practice as market remedies with the aim of countering the market power of the dominant telecommunications operator (usually the incumbent). They may apply on the access market at any of the following stages: before a request for access,³ where an access agreement is being negotiated,⁴ or in the case where an access agreement has been negotiated in conjunction to the specific requirements as set down by the National Regulatory Authorities (NRA) to meet reasonable requests for access.⁵ However, in practice, SMP designated operators often block the application of these *ex-ante* remedies on the market by simply failing to respect the obligations as found in the Access Directive which are imposed upon them by the NRA's. Alternatively, such SMP designated operators may simply frustrate the effectiveness of these remedies to the market by either exploiting their application, or by demonstrating a lack of will or a failure to fully comply with them, a practice known as “*creeping compliance*”.⁶ Consequently, NRA's are frequently required to intervene on the market in an *ex-post* regulatory capacity, either in response to representations and complaints made

² See Directive 2001/19EC of the European Parliament and of the Council of 7 March 2002 on access to, and interconnection of, electronic communications networks and associated facilities (Access directive). and 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 and services (Framework Directive), Art. 14.

³ See Arts. 9, 11, & 13 of Directive 2001/19EC of the European Parliament and of the Council of 7 March 2002 on access to, and interconnection of, electronic communications networks and associated facilities (Access directive).

⁴ *Ibid*, see; Art. 12 (1)(b).

⁵ *Ibid*, see; Art. 12.

⁶ See Ariel Ezrachi, *Under (and Over) Prescribing of Behavioral Remedies*, The University of Oxford Centre for Competition Law and Policy, Working Paper (L) 13/05. A good example of the “*creeping compliance*” of an incumbent operator in possession of essential infrastructure and network with an access obligation concerns the obligation to negotiate access in “*good faith*” as provided for in Art. 12(1)(b) of the Access Directive (obligation of access to, and use of, specific network facilities). As there is no way to check the motivation of an incumbent operator while negotiating, there is nothing to prevent an incumbent from negotiating in “*bad faith*” to delay, frustrate or prevent the conclusion of the access agreement. Another example of such “*creeping compliance*” may be found in the context of the obligation to publish a reference offer under Art. 9(2) of the Access Directive (obligation of transparency). While not breaching this obligation, SMP designated operators sometimes publish reference offers which bear no relation to market conditions. Because the relevant NRA is then obliged to formulate a correct reference offer, this tactic slows down the process concerning the granting of fair and reasonable access.

by operators on the market,⁷ or by means of unilateral intervention where justified,⁸ in order to correct the anti-competitive practices of the non-compliant market operator. In addition to this, any discriminatory behavior of an operator towards competitors on the access market can only be addressed through the application of *ex-post* regulatory remedies following similar representations and complaints from competitors. In response, National Competition Authorities (NCA's) may also choose to concurrently apply competition law principles under Art. 82 EC Treaty on the telecommunications market alongside sector specific regulation.⁹ Experience has shown however, that, while NCA's and the European Commission alike have imposed heavy financial penalties on operators found abusing their position of dominance on the access market,¹⁰ such fines do not function as sufficient deterrents. From the perspective of alternative market operators, such fines often only come after lengthy (and costly) legal proceedings, by which time the dominant operator in possession of the essential infrastructure has already gained an irreversible competitive advantage over the other operators on the market. Consequently, it is often the case that the application of *ex-post* competition law principles is insufficient to remedy or to correct the competitive imbalance which may be effected on the market in the mean-time.

In practice therefore, fair and reasonable access to essential telecommunications network and facilities is often only ensured through the application of *ex-post* obligations to the market. This is because, in the event of the failure in the application of *ex-ante* remedies, an NRA has only recourse to *ex-post* regulatory measures, which apply after the abuse has taken place. This creates a situation which is in fact, closer to market regulation by means of the application of competition law principles, rather than regulation by *ex-ante* sector specific principles as provided for by the EU Regulatory Framework. The problem with this situation is that *ex-post* regulation is only suitable

⁷ See Directive 2002/21/EC of the European Parliament and of the Council of 7th March 2002 on a common regulatory framework for electronic communications networks and services, Art. 20, and 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, Art. 5(4).

⁸ 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, Art. 5(4).

⁹ The Court of First Instance (CFI), and the ECJ have consistently held that competition rules may apply concurrently with sector-specific legislation where the sector-specific legislation does not preclude the undertakings that it governs from engaging in autonomous conduct that prevents, restricts, or distorts competition. See; Court of Justice in Joined Cases C-359/95 and C-379/95 P *Commission and France v Ladbroke Racing* [1997] ECR I-6225, paragraph 34, with further references; Court of First Instance in Case T-228/97 *Irish Sugar v Commission* [1999] ECR II-296, paragraph 130; Court of First Instance in Case T-513/93 *Consiglio Nazionale degli Spedizionieri Doganali* [2000] II-1807, paragraphs 59 et seq. See also; Commission Decision of 21 May 2003 relating to a proceeding under Article 82 of the EC Treaty (Case COMP/C-1/37.451, 37.578, 35.579 – Deutsche Telecom AG) par. 54.

¹⁰ See for example; French Conseil de la Concurrence) Case no 05-D-51 of Nov. 7th 2005 (Neuf Telecom), European Commission; Case COMP/C-1/37.451, 37.458, 37.579 – (Deutsche Telekom), European Commission; Case COMP/38.233 – (Wanadoo), Case T-340/03 (*France Telecom v Commission*).

on markets where competition is at a mature stage, and this is not yet the case in relation to telecommunications markets. While it is recognised that such markets are currently between the inter-mediate and advanced stages of liberalisation, years of State monopolization of the sector has resulted in a huge difference in the market powers of separate telecommunications operators. This has led to an inherent competitive imbalance on telecommunications markets between operators, which makes the abuse of dominance not only a likelihood, but a certainty. Given such particular conditions, it is submitted that reliance on *ex-post* remedies to correct anti-competitive practices specifically on access markets is wholly insufficient. Consequently, a legal framework which provides for the prevention of the abuse of dominance, rather than the correction or remedying of the particular anti-competitive situation caused by the commission of such an abuse of dominance, is therefore highly necessary!

The application of a structural remedy to the access market;

In response to the difficulty encountered with the application of *ex-ante* remedies, alternative operators, as well as some NRA's,¹¹ are currently considering the logic of applying a structural remedy to address anti-competitive practices on the access market. A forced wholesale-retail split in the actual structure of the dominant telecommunications operator in possession of the bottleneck monopoly is currently being advocated as a more effective means of preventing discriminatory practices concerning the granting of access to essential network and facility. Essentially, the imposition of such a measure, known as *operational separation* as an SMP obligation on a telecommunications operator eliminates the actual economic incentive of such an operator to set unfair terms of access. In a case where operational separation is imposed as a remedy, a telecommunications operator would be obliged, by means of the non-discrimination obligation as found in the Access Directive,¹² to offer the same terms of access to its own vertically integrated retail arm as it offers to third party competitors on the market, or vice versa. Such a split in the operations of an SMP designated network operator would, in practice, effectively function as a preventative mechanism, rather than as a remedial measure. While the latter can only aim at correcting the competitive imbalance brought about by the abuse of dominance, it is submitted that a preventative measure such as operational separation is significantly more effective as a remedy as it prevents the anti-competitive structure of a market from facilitating the abuse of dominance, and the breach of fair competition practices. It is however important to bear in mind

¹¹ See section entitled: "*Operational separation in practice as a market remedy*", p. 6.

¹² 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, Art. 10(2).

that, because of the draconian nature of operational separation, such a remedy should only be applied in conjunction with the principle of proportionality, and on a case-by-case basis after the conclusion of a thorough cost benefit analysis.

Operational separation differs as a market remedy from current *ex-ante* access obligations in that the former is a structural remedy, while the latter are quasi-behavioral remedies. Structural remedies, while more draconian in nature, are favored by many as a more effective means of market regulation. They can be seen as preventative measures rather than correcting measures, as they aim at the rectification of the market imbalance itself, rather than the resolution of the anti-competitive effects which come from the anti-competitive structure of the market.¹³ Their timely implementation and permanent nature are also considered as more favorable to the entry of new market entrants, as well as to the status of existent competitors on the market. Additionally, structural remedies require less post-implementation monitoring than do behavioral remedies, and are also generally more cost-efficient.¹⁴ Behavioral commitments, are, when applied to the market, less effective however. Contrary to structural remedies, there is a risk that their complexity may result in loopholes which the SMP designated telecommunications operators may take advantage of, whilst not constituting a blatant breach of the commitment.¹⁵ By their nature, such commitments are also more vulnerable to manipulations and may be eroded of their effectiveness. Additionally, indirect costs may also occur when the behavioral remedy results in the distortion of competition and the generation of market inefficiencies, as is the case when such a remedy is applied over a long period of time and involves direct market intervention by a regulatory body. Such remedies may also affect the incentives in the market or may provide potential market entrants and competing undertakings with a distorted picture of barriers to entry, potential competition and profitability.¹⁶

What is operational separation?

¹³ Vertical and horizontal divestitures are the most common form of structural remedy which are applied onto a market. In essence, a divestiture seeks to remedy the competitive imbalance caused to a market by a merger by either strengthening an existing source of competition on the market through the disposal of assets to a third party market participant independent of the merging parties, or by creating a new source of competition through the disposal of some of the business or assets to a new market entrant. Other examples of structural remedies include: hold separate provisions, representations and warranties, and “*crown jewel*” provisions. Quasi-structural remedies are also sometimes applied to the market, and include: the licensing of intellectual property, the removal of anti-competitive contract terms, the granting of non-discriminatory access to networks and the removal or reduction of quotas, tariffs, or other regulatory impediments.

¹⁴ See Ariel Ezrachi, *Under (and Over) Prescribing of Behavioral Remedies*, The University of Oxford Centre for Competition Law and Policy, Working Paper (L) 13/05, pp. 1 & 2.

¹⁵ *Op. cit.*, note 6.

¹⁶ Ariel Ezrachi, *Under (and Over) Prescribing of Behavioral Remedies*, The University of Oxford Centre for Competition Law and Policy, Working Paper (L) 13/05, p. 3.

The aim of operational separation is essentially to create two separate entities, one which will provide the core bottleneck wholesale services, and the other which will provide the downstream retail services, without actually interfering with the ownership of the business.¹⁷ While such a separation of operations interferes with the vertical integration of an undertaking on the market, the long term economic consequences of such a remedy for the telecommunications operator are not negative. It is submitted that, in spite of interfering with its ability to price discriminate, a wholesaler can be as profitable as a vertically integrated entity on the market. There is nothing to prevent the wholesaler from demanding competitive prices on the access market, which could feasibly off-set any potential loss caused by the operational split.¹⁸ It is also submitted that a structural remedy which could guarantee equal terms of access to essential bottleneck monopoly to all telecommunications operators would benefit both existent competitors, as well as new market entrants, and would create a framework whereby fair competition on the access market would finally be both realisable and sustainable. The potential welfare benefit which would then be passed downstream onto the service and consumer markets is significant.

Importantly however, operational separation should not be confused with the more draconian remedy; *structural separation*. What distinguishes both remedies is the fact that structural separation concerns the actual form of ownership of the business,¹⁹ while, under operational separation, both the wholesale and retail arm of the operator remain under the same ownership despite the fact that both function or operate separately. Structural separation is however perceived as an extreme measure by those in industry, as well as in those concerned with the regulation of the sector. In its 2006 Impact Assessment Study on the review of the current EU Regulatory Framework,²⁰ the European Commission concluded that structural separation, as a remedy, is rarely

¹⁷ Operational separation may take many different forms. One such form requires the businesses to be legally separate entities. A further, and more draconian step before moving to full ownership separation of these businesses, would be to open the separated access business up to minority shareholders. There is the argument that such a constellation would lead to a modification in the access businesses' economic incentive to discriminate, as it would not necessarily be in the minority shareholders' interests to favour the downstream business of the majority shareholder.

¹⁸ See generally Anupam Banerjee, Marvin Sirbu, *FTTP Industry Structure, Implications of a wholesale retail split*, Carnegie Mellon University, Pittsburgh, Pennsylvania 15213, USA.

¹⁹ Structural separation may take any of the following forms;

Separation of network operators into smaller networks, each connected to a group of consumers (such as the splitting up of an incumbent company into several regional companies, each providing local services to a group of consumers);

Separation of the non-competitive parts of network operators (particularly, the "last mile" of the connection to the customer) from the competitive parts (such as long-distance services);

Separation of network operators on the basis of technology used to connect to consumers (such as the separation of local telecommunications companies based on copper-wire from companies using cable TV networks or those using cellular services).

²⁰ *Commission Staff working document, Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions on the Review of the EU Regulatory Framework for electronic communications networks and services*, {COM(2006)334 final} Impact Assessment, Brussels 28 June 2006. The OECD reports cited by the Commission in the impact assessment study also treat the imposition of structural separation as a remedy in the communications sector as unjustified. See;

justified. The Commission paper went on to state that the risk posed by such a remedy to the Internal Market was too great as the NRA solutions and practices would vary widely in respect to the utilisation of this remedy. The Commission also expressed concern from an economic point of view, stating that the cost-benefit calculation for this obligation would be very likely to bring negative results, and a measure like this would not be in harmony with the proportionality principle. Neither would this measure solve the regulatory problem, as network service providers would still have to be forced by regulation to offer prices and conditions facilitating competition.²¹ The author also highlights the in-compatibility of the forced structural separation of an entity with the right of ownership, which is a fundamental value in most European constitutional orders.

Operational separation in practice as a market remedy;

While the imposition of structural remedies on the market lies outside of the scope of today's EU Regulatory Framework,²² it is a current practice under EC Competition law under Council Regulation 1/2003.²³ Additionally, NRA's in some Member States (MS) are already investigating the possibility of introducing operational separation onto the market as a tool of national competition law. The Office of Communications (Ofcom), the United Kingdom NRA, has already agreed with British Telecom (BT) on a number of undertakings which concern the operational separation of the latter's wholesale activities from its retail activities.²⁴ In this way

DAFFE/COMP/WP2 "The benefits and costs of structural separation" – Note by TISP, of 10.01.2003 and DSTI/ICCP/TISP(2005)10 "Draft Report to Council on experiences with structural separation" of 28.10.2005.

²¹ Commission Staff working document, Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions on the Review of the EU Regulatory Framework for electronic communications networks and services, {COM(2006)334 final} Impact Assessment, Brussels 28 June 2006, p. 11.

²² The concept of a "structural remedy" is closely associated with the EC competition law concept of "structural harm" on the market. This was first developed by the ECJ in the case of *Continental Can*. In this case it was determined that the distinction between measures which concern the structure of the undertaking and practices which affect the market is not decisive, for any structural measure may influence market conditions if it increases the size and the economic power of the undertaking. See C-6/72, *Europemballage Corporation and Continental Can Company Inc. v Commission of the European Communities*, par. 21.

²³ See Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 & 82 of the Treaty, recital 12, & Art. 7. This Regulation makes explicit provision for the Commission's power to impose any remedy, whether behavioral or structural, which is necessary to bring an anti-competitive practice effectively to an end. Importantly however, Art. 7 also states that structural remedies should only be imposed either where there is no equally effective behavioral remedy or where any equally effective behavioral remedy would be more burdensome for the undertaking concerned than the proposed structural remedy. It also states that the principle of proportionality in the application of the remedy should be respected.

²⁴ Specifically, section 370 of the Communications Act 2003 gives Ofcom concurrent functions with the Office of Fair Trading under Part 4 of the Enterprise Act 2002. Accordingly, under Section 131 (Part 4) of the Enterprise Act 2002, Ofcom may now make a market investigation reference to the Competition Commission where

"... it has reasonable grounds for suspecting that any feature, or combination of features, of a market in the UK for goods or services prevents, [in this case the telecommunications market] restricts or distorts competition in connection with the supply or acquisition of any goods or services in the UK or a part of the UK."

However, Under Section 154 of the Enterprise Act, instead of making such a reference, but where it has the power to make one and otherwise intends to do so, Ofcom may accept undertakings from such persons as it considers appropriate, to take such action as it considers appropriate. These undertakings must be for the purpose of remedying, mitigating or preventing any adverse effect on competition concerned, or any detrimental effect on customers so far as it

Ofcom has been able to extract certain binding undertakings from BT concerning the operational separation of the enterprise's activities which are in fact outside of, and complementary to, the EU Regulatory Framework. The Swedish NRA is also considering the implementation of operational separation as a remedy on its national telecommunications market. In a document concerning proposals for a new national broadband strategy dating from February 15th 2007, the Swedish NRA, Post-och Telestyrelsen (PTS), included the proposal for the functional as well as the legal separation of the incumbent as a possible policy trajectory to achieve certain stated goals and objectives.²⁵ Outside of the EU, New Zealand passed legislation in late 2006 establishing a framework for the operational separation of Telecom New Zealand into a network access arm, a wholesale arm and a retail arm.²⁶ The bill also allowed for an independent oversight group to make sure that competitors who use Telecom New Zealand's service get fair and equal access.²⁷ Australia passed similar legislation one year previously in 2005,²⁸ and on June 23rd 2006, the Australian Minister for telecommunications approved the draft plan for operational separation furnished by the Australian incumbent, Telstra.²⁹

Operational separation and the review of the EU Regulatory Framework;

As part of the current review of the 2002 EU Regulatory Framework, the European Commission has begun to consider the operational separation of vertically integrated

has resulted from, or may be expected to result from, the adverse effect on competition. In the case of BT, these undertakings concerned a commitment from BT to bring about the operational separation of the wholesale part of the enterprise from the retail part.

²⁵ See <http://pts.se/Dokument/dokument.asp?ItemId=6541> (last visited on March 1st 2007). PTS has strongly indicated that, in order to achieve long-term and sustainable competition on the broadband market, it wishes that all operators can gain access to the fixed incumbent TeliaSonera's local access network on equal terms. In order to dispel any favoritism, PTS intends that TeliaSonera's retail organisation should have the same access rights to TeliaSonera's network as other service providers have. PTS has stated that the most suitable means to prevent the incumbent from favoring its retail division is to adopt the "operational separation" model and/or "a stronger legal separation" between the wholesale and retail arms of TeliaSonera. PTS hopes that this will reduce inertia on the market, as well as improving predictability. PTS has also stated that it is convinced that such separation should be based on the traditional divisions used at TeliaSonera, with TeliaSonera Network Sales AB addressing only operators (i.e. wholesale) but not end users.

²⁶ Telecommunications Amendment Bill, part 2AA.

²⁷ It is important to note that not all NRA's consider that it is possible to apply operational separation as a market remedy. On the 2nd March 2007, the Dutch NRA Onafhankelijke Post en Telecommunicatie Autoriteit (OPTA) published a study on the UK approach to functional separation of BT. Importantly, the study concluded that neither OPTA nor the Dutch NCA currently have direct powers to impose such separation. The report did however acknowledge that Art. 6a.11 of the Dutch Telecommunications Law provides a possible opening, but that invoking this article requires a prior Ministerial Decision. The report further stated that, after the review of EU directives, and their transposition into Dutch law (in 2009-2010), a functional separation remedy may become available. The report reaffirmed the importance of proportionality when applying this remedy which will have to be assessed in the context of market analyses.

²⁸ Operational separation was implemented as a statutory condition of Telstra's carrier license, specified in part 8 of Schedule 1 of the Telecommunications Act, 1997, Act No. 47 of 1997 as amended.

²⁹ See http://www.dcita.gov.au/communications_for_business/funding_programs_and_support/connect_australia/operational_separation (last accessed on March 2nd 2007).

telecommunications operators in possession of bottleneck monopoly as a possible access remedy. In a keynote speech delivered on November 16th 2006, Commissioner Reding referred to operational separation while addressing competition problems associated with vertically integrated firms. The Commissioner specifically referred to measures already undertaken in the UK, stating that the provision of equivalence of treatment to all operators could be achieved by adding operational separation as a possible remedy under the EU Regulatory Framework. Ms. Reding stated that operational separation could serve to make competition more effective in a service-based competition environment where infrastructure-based competition is not expected to develop in a reasonable period.

Importantly however, the Commissioner stated that such operational separation may only be a useful remedy in specific cases, and that it is not something which may be applied in a general manner on the telecommunications market. Ms. Reding affirmed that a cost benefit analysis must be made on a case-by-case basis before such a remedy is imposed, the effects of imposing such a remedy in Europe's Internal Market must also be taken into consideration in each individual case.³⁰

Industry has also been favorable towards the inclusion of operational separation as a remedy in the reviewed EU Regulatory Framework. In response to the Commission call for input in 2006 concerning the review of the EU Regulatory Framework, the European Competitive Telecommunications Association (ECTA) argued that the EU Regulatory Framework should fill this gap

“...by clearly making specific provisions for regulators to promote compliance through organizational means including the ability to require the creation of quasi-independent organizational divisions with objectives and management incentives that do not reflect the vertically integrated nature of the wider business.”³¹

³⁰ Viviane Reding, Member of the European Commission responsible for Information Society and Media, *From Service Competition to Infrastructure Competition: the Policy Options Now on the Table*, ECTA Conference 2006 Brussels, 16 November 2006. Available at: <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/06/697&format=HTML&aged=0&language=EN&guiLanguage=en> (last visited on March 1st 2007).

Specifically, the Commissioner used the following phraseology: “[Operational separation] may be a useful remedy in specific cases. It is certainly not a panacea.”

³¹ ECTA, Part I: 2006 review: Call for Input Legislative Aspects, p. 26. Interestingly, ECTA made reference to Art. 10 of Directive 2003/54/EC in its submission which concerns rules for the Internal Market in electricity; (Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the Internal Market in electricity and repealing Directive 96/92/EC) This article specifically provides that, were the transmission system operator is part of a vertically integrated undertaking, it shall be independent at least in terms of its legal form, organisation and decision making from other activities not

Conclusion;

A vertically integrated telecommunications operator has strong incentives to use its powerful advantages at wholesale level and all the tools at its disposal, whether legal, technical or economic in nature, to delay, to lower the quality, or to raise the price of access in order to leverage its dominance onto downstream retail service markets. Experience has shown that reliance on the quasi-behavioral *ex-ante* access remedies found under the current EU Regulatory Framework does not prevent such operators in possession of bottleneck monopoly from abusing their positions of dominance on the access markets. Such anti-competitive practices allow dominant operators to get a competitive head-start on down-stream retail markets, as well as benefiting from first mover advantage on new and emerging markets. Recourse by NRA's or NCA's to *ex-post* market remedies or to competition law principles is however proving insufficient to redress the imbalance brought about by the refusal to supply, as well as the commission of other discriminatory practices, on the access market. While such principles are effective on markets where competition is at a mature stage, the application of only *ex-post* measures on markets which are undergoing liberalisation is wholly insufficient. By effecting a long term split in the internal structure of a telecommunications operator, the author submits that operational separation makes it economically unfeasible for the telecommunications operator in possession of the bottleneck monopoly to discriminate against competitors, and essentially forces it to offer equivalence of access to all market operators. Therefore, rather than applying after the abuse has already occurred, as is the case with *ex-post* competition law principles, operational separation functions as a preventative mechanism as it eliminates the incentive of the operator in possession of the infrastructure to offer unfair or unreasonable terms of access. Also important is the fact that because operational separation is a structural remedy, it will not face the same compliance problems as *ex-ante* access behavioral or quasi-behavioral remedies face when applied to the market. However, it must be stressed that, while operational separation is more effective in form and nature than the current *ex-ante* access remedies, it is also a more draconian measure. Pending on national MS law, NCA's may choose to pursue the application of this measure as a structural remedy under competition law. Alternatively, in the case that there is no such provision for this under national law, NCA's may leave this competence to the Commission under Regulation 1/2003. What must

relating to transmission. These rules shall not create an obligation to separate the ownership of assets of the transmission system from the vertically integrated undertaking. This provision could be referred to in the context of the reviewed Telecommunications Framework.

be remembered however is that operational separation should only be applied as a remedy under the principle of proportionality, on a case-by-case basis, and only when necessary. It is the opinion of the author that the inclusion of operational separation in the reviewed EU Regulatory Framework as a market remedy would be a good means of ensuring such proportional application of this measure on the market, as the European Commission would effectively have the last say in sanctioning or vetoing such a remedy under Art. 7 of the Framework Directive.³² Recent statements from Commissioner Reding have indicated that the inclusion of operational separation as a remedy under the reviewed EU Regulatory Framework is a possibility. While this is a most welcome development, it is hoped that, if this is to be the case, the Commission will constructively draw from the experience on markets where operational separation has already been implemented as a remedy.

³² While Regulation of 1/2003 allows for a system of co-operation between the NCA's and the Commission, it does not provide the Commission with a power of veto over decisions of the NCA as does Art. 7 of the Framework Directive. Art. 11(4) of Regulation 1/2003 obliges NCA's to inform the Commission with a summary of a case which it is presiding over, a summary of the envisaged decision, and in the absence thereof, any other document indicating the proposed course of action, while Art. 11(5) allows the NCA's to consult the Commission on any case involving the application of Community law.