Margin Squeeze as Abuse of Dominant Position on Networks

Annotation on the Judgment of the General Court (Eighth Chamber) of 29 March 2012 in case T-336/07, Telefónica SA, *Telefónica de Espana vs European Commission.* Application dismissed by the General Court on substantial grounds, especially regarding alleging errors of law in the application of Article 82 EC (abusive conduct) and an alleging ultra vires application of Article 82 EC.

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I. Introduction

Telefónica brought the case before the General Court seeking the annulment of the decision of the European Commission ("Commission") which found that Telefónica had abused its dominant position in the Spanish market for wholesale access to its network at a regional and national level by imposing unfair prices on competitors and levied on Telefónica a total fine of € 151 million ("Commission Decision").

Following settled case-law, the Court decided that in order to examine the alleged dominant position of an undertaking on a given network and, subsequently, any product market, *the level of competition had to be seen in the context of a particular market.* This market comprises all those products which, due to their characteristics, are specifically suitable for satisfying the constant needs of the consumers and are to a small extent substitutable with other products.

In order to measure the relevant economic facts, we need to take account of a fixed alternative operator, which replaces the regional wholesale access with the local loop unbundling, in addition to concluding a RUO (Reference Unbundling Offer) and should also materialize the necessary investment to develop its network. As the Commission said (and the Court confirmed) we should also take account of the fact that this operator will only be able to reap the benefits of this investment after it has attracted a sufficient client base, something which is not certain nor immediate. The key issue that must be assessed in an investigation is therefore whether the incumbent would be able to offer retail services to its customers with an adequate profit (or at least without losses) if he had to pay the wholesale prices imposed to its competitors.

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II. Relevant facts – The Commission's Decision

Telefónica, SA, is a former State monopoly in the telecommunications sector in Spain. Between September 2001 and December 2006, which was the period concerned by Commission Decision,[1] Telefónica supplied broadband services through its subsidiary Telefónica de España, SAU ('TESAU'). Before the full liberalisation of the telecommunications markets in 1998, Telefónica was owned by the Spanish State and had a legal monopoly in the retail provision of fixed-line telecommunications services. Currently, it operates the only nationwide fixed telephone network and in the period concerned holds a 84 % share of the relevant market.

On 11 July 2003, Wanadoo España, SL (now France Telecom España, SA) submitted a complaint to the Commission of the European Communities, claiming that the margin between the wholesale prices which the subsidiaries of Telefónica charged their competitors for the wholesale supply of broadband access in Spain and the retail prices which they charged end-users was not sufficient to allow competitors of Telefónica to compete with it.

On 4 July 2007 the Commission adopted the contested decision forming the subject-matter of this

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1 C(2007) 3196 final of 4 July 2007 relating to a proceeding pursuant to Article 82 [EC].

action. The Commission identified three relevant product markets, namely one retail broadband market (ADSL) and two wholesale broadband markets. As regards the wholesale markets, the Commission stated that three main wholesale offers were available through Telefónica's network, namely a reference offer for local loop unbundling, marketed solely by Telefónica, a regional wholesale offer (GigADSL; 'the regional wholesale product'), also marketed solely by Telefónica, and several national wholesale offers marketed by Telefónica (ADSL-IP and ADSL-IP Total; 'the national wholesale product') and by other operators on the basis of local loop unbundling and/or the regional wholesale product.

The Commission considered that the regional wholesale product and local loop unbundling were not substitutable. As a basis for that conclusion, the Commission referred, with respect to demand-side substitutability, to significant network roll-out investments and to the functional differences between the two types of wholesale access. Switching from a regional wholesale product to the national wholesale product would not make economic sense, since it would be irrational and unlikely that operators that have already invested in the roll-out of a network would bear the cost of not using their network and using the national wholesale product which would not give them the same possibilities with respect to control of the quality of service of the retail product as the regional wholesale product.

As regards supply-side substitutability, the Commission observed that while, admittedly, an operator wishing to provide a national wholesale offer could do so on the basis of the regional wholesale offer, which would entail considerable investments, those investments bore no comparison with the investment necessary for the local loop unbundling which was required upstream in order for the operator to be able to offer a regional wholesale access product that would compete with Telefónica's.

Following its settled view regarding access to networks, the Commission said that the NRAs need to carefully follow and evaluate developments in order to ensure that appropriate access remedies are maintained for the forward-looking periods for which competition is judged to be ineffective, and to avoid undermining or discouraging efficient entry. Remedies on networks such as duct sharing, access to dark fiber, mandated backhaul from the street cabinet and new forms of bitstream access, could be considered where these are appropriate. This may call for some transitional arrangements to be considered, to allow time for adaptation of existing business models.[2]

The Commission also considered that broadband access technologies other than ADSL, and in particular cable, could not be regarded as substitutable for ADSL offers. Even though it was technically possible for cable operators to provide wholesale broadband access to third parties equivalent to the national and regional wholesale products, practical and economic difficulties would prevent them from doing so, so that such an offer would not be economically viable.

The Commission concluded that Telefónica had a monopoly in the supply of the regional wholesale product and more than 84 % of the national wholesale product market. Telefónica also had a dominant position on the retail market. The Commission considered that Telefónica had infringed Article 82 EC [now 102 TFEU] by imposing unfair prices on its competitors in the form of a margin squeeze between the prices for retail broadband access in the Spanish 'mass market' and the prices on the regional and national wholesale broadband access markets, throughout the period from September 2001 until December 2006.

As regards the method of calculating the margin squeeze, the Commission considered (i) that the efficiency of Telefónica's competitors had to be measured against Telefónica's downstream costs (the 'equally efficient competitor' method), (ii) that the appropriate method for the evaluation of costs was, in the present case, that of long-run average incremental costs ('LRAIC'), (iii) that the assessment of profitability over time could be established by two methods, namely the so-called 'period-by-period' method and the discounted cash flow ('the DCF') method, (iv) that the margin squeeze had to be calculated on the basis of the range of services marketed by Telefónica in the relevant retail market, and (v) as regards the choice of upstream inputs for the calculation of whether the downstream prices could be reproduced, that Telefónica's tariffs had to be capable of reproduction by an as-efficient competitor using at least one wholesale product of Telefónica in each of the relevant wholesale markets. The Commission calcu-

2 European Commission, Explanatory note SEC(2007) 1483 final. Accompanying document to the Commission Recommendation on Relevant Product and Service Markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services (Second edition) {(C(2007) 5406)}.

lated whether the difference between Telefónica's upstream and downstream prices covered at least Telefónica's downstream LRAIC.

By applying the above methodology the Commission calculated that Telefónica's retail prices could not be reproduced on the basis of its national or regional wholesale products between September 2001 and December 2006. As regards the effects of the abuse, the Commission considered that Telefónica's conduct had probably restricted the network capacity of ADSL operators to achieve sustainable growth in the retail market and had probably harmed the interests of end-users. So a fine had to be imposed.

The starting amount of the fine, € 90.000.000, takes account of the fact that the gravity of the abusive practice became clear over the period under consideration and, more particularly, after the adoption of the Deutsche Telekom decision.[3] A multiplier of 1.25 was applied to that amount to take account of Telefónica's significant economic capacity and to ensure that the fine was sufficiently deterrent, and the starting amount of the fine was thus increased to € 112 500 000. The infringement had lasted from September 2001 until December 2006, that is to say, for five years and four months, the Commission increased the starting amount of the fine by 50 %.

3. The case before the Court – Arguments of the parties

The applicants put forward a number of claims, seeking annulment of the contested decision:

(a) breach of the rights of the defense,
(b) errors of fact and of law in the definition of the relevant wholesale markets,
(c) errors of fact and of law in the establishment of Telefónica's dominant position on the relevant markets,
(d) errors of law in the application of Article 82 EC as concerns Telefónica's abusive conduct,
(e) errors of fact and/or errors of assessment of the facts and errors of law with respect to Telefónica's abusive conduct and its anti-competitive impact, and
(f) an *ultra vires* application of Article 82 EC and breach of the principles of subsidiarity, proportionality, legal certainty, sincere cooperation and sound administration.

Principally, the Court in this case does not seem to alter the landmark view of the ECJ in cases *Deutsche Telekom v Commission* and *TeliaSonera.*[4] Before the margin squeeze is condemned as unlawful, the potential anti-competitive effects must be demonstrated. Margin squeeze must be analyzed as the resulting obligation in consistency with the Commission Guidelines.[5]

At this point, a brief retrospective of 30 years network market regulation appears necessary. It is a fact that the telecommunications networks have been subjected to extensive regulation in the last three decades, in an effort to complete the pan-European liberalization of markets. It all started with an ECJ decision of 1985[6] which stated that competition rules did apply to the telecommunications networks. The European Commission, in its 1987 Green Paper, then established the need to liberalize telecommunications networks as a vital step to ensuring the competiveness of the European market. The first regulatory instruments adopted were the Terminal Equipment Directive,[7] the Services Directive[8] and, of course, the very important Open Network Provisions.[9] Then followed Directive 97/51/EC on the application of ONP in a competitive environment,[10] Directive 97/33/EC on Interconnection, and the Directive replacing the previous ONP voice telephony Directive to take account of the introduction of full competition in telecommunications services and infrastructure (Directive 98/10/EC). The goal of the ONP was first to allow access to the relevant networks and services to new market entrants (liberalization) and second to create a single European telecommunications market (harmonization). Accordingly, even though the main target was the liberalization of the market(s), a significant part of the ONP was devoted to harmonize infrastructure

3 Case C-280/08 P *Deutsche Telekom* v *Commission* [2010] ECR I-9555.

4 Case C-52/09 *TeliaSonera* [2011] ECR I-0000.

5 Communication from the Commission – Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings (2009/C 45/02).

6 Case 41/83 *Italy v Commission* (UK intervening), 1985 ECR 510.

7 Commission Directive 88/301, OJ 1988 L 131.

8 Commission Directive 90/388. OJ 1990 L 192.

9 Directives 92/44/EEC and 95/62/EC for the harmonisation of conditions for open and efficient access to, and use of, the leased lines provided on public telecommunications networks and voice telephony respectively.

10 OJ 1997 L 295/23.

use, network interfaces, network usage and national tariffs.[11]

The work of the NRAs is not easy at all with telecoms networks. A vast variety of products and services, the complex bundle offers and the upcoming Convergence (that led to double, triple and quadruple telecoms products) created a lot of confusion and complexity in defining markets and relevant products. The first relevant markets that were identified and regulated within the ONP directives were (i) Fixed telephony, (ii) Mobile telephony, (iii) Leased lines and (iv) Interconnection. SMP was set at the market share of 25 % and the obligations of the SMP operators were transparency in pricing, accountant separation, non-discrimination, open access and an approved Reference Interconnection Offer (RIO). The 2002 Regulatory Framework shifted the center of regulation from liberalization to harmonization. The target of a single European telecoms market became clearer, as did the need for identifying the new relevant markets emerging from the Converged environment. It became clear that in order to define those relevant markets, more *ex-ante* regulation would be needed as well as, of course, all the instruments that could be borrowed from the traditional Competition Law. Competition has started to be somehow effective now, in comparison with the previous decade, so "significant market power" (SMP) got an upgrade and was equated, in the new regulatory framework, with the concept of dominance under Article 82 of the EC Treaty. Accordingly, the *"hypothetical monopoly test"* was introduced by the Commission in its guidelines of 2002[12] (which are still the main instrument for defining and assessing SMP[13]).

In principle, the "hypothetical monopolist test" is relevant only with regard to products or services, the price of which is freely determined and not subject to regulation. Thus, the working assumption will be that current prevailing prices are set at competitive levels. If, however, a service or product is offered at a regulated, cost-based price, then such price is presumed, in the absence of indications to the contrary, to be set at what would otherwise be a competitive level and should therefore be taken as the starting point for applying the "hypothetical monopolist test". In theory, if the demand elasticity of a given product or service is significant, even at relative competitive prices, the undertaking in question lacks market power. If, however, elasticity is high even at current prices, that may mean only that the undertaking in question has already exercised market power to the point that further price increases will not increase its profits. In this case, the application of the hypothetical monopoly test may lead to a different market definition from that which would be produced if the prices were set at a competitive level.

In fact what the guidelines say is that we should measure how probable it would be for the consumers and the competition to switch to another product market (substitutability) in case of an increase of 5-10 % is applied on a certain market product, That test, though, presupposes freely set prices and, certainly, no regulated ones. Any assessment of market definition must therefore take into account this potential difficulty. However, *"NRAs should proceed on the basis that the prevailing price levels provide a reasonable basis from which to start the relevant analysis unless there is evidence that this is not in fact the case"*[14].

Since the cable networks have been identified as a major contributor to national economies, where an incumbent is activated (and owns the sole national-wide network) any possibility for anti-competitive behavior directly affects the cost for the competition (that means the fixed alternative operators) and the dynamics of the economy. Hypothetical monopoly test shall include margin squeeze as one of the most typical means of competition distortion when it comes to pricing imposed by a vertically integrated network owner with a dominant position (significant market power – SMP). Margin squeeze means that this undertaking may charge a price for the product on the upstream market which, compared to the price it charges on the downstream market, does not allow, even an equally efficient, competitor to trade profitably in the downstream market on a lasting basis. In e-communications networks, the margin squeeze benchmark, which the Commission will generally rely on to determine the costs of an equal-

11 Viktor Mayer Schonberger and Matias Strasser: "A closer look at Telecom Deregulation: The European Advantage" *Harvard Journal of Law and Technology,* Volume 12, Number 3, Summer 1999.

12 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)

13 See Court press release No 47/11 regarding Case C-410/09 *Polska Telefonia Cyfrowa sp. z o.o. v Prezes Urzędu Komunikacji Elektronicznej,* available at *http://curia.europa.eu/jcms/upload/docs/application/pdf/2011-05/cp110047en.pdf* , accessed 18.09.2013.

14 See par. 42 of the aforementioned Commission Guidelines (note 12).

ly efficient competitor are the LRAIC of the downstream division of the integrated dominant undertaking.[15] Usually on this course, an undertaking sets higher wholesale prices combined with lower retail prices (through bundle offers) – but not necessarily under the cost, to its own customers, thus making the access to its network highly unprofitable for the competition.

a. Market Definition and Dominant Position

The Court, following the settled case law, rejected all the defendants' arguments by pointing out that for the purposes of investigating the possibly dominant position of an undertaking on a given product market, the possibilities of competition must be judged in the context of the market comprising the totality of the products which, with respect to their characteristics, are particularly suitable for satisfying constant needs and are only to a limited extent interchangeable with other products. Moreover, the competitive conditions and the structure of supply and demand on the market must also be taken into consideration.[16]

The Commission had not failed to calculate the profits resulting from the use of the local loop (higher revenues, diversity of final retail services and technological independence of Telefónica) because an alternative operator wishing to switch from regional wholesale access to local loop unbundling will have to make the investments necessary to roll out its network, but will reap the benefits of that switch *"only after having achieved a sufficient customer base, which is neither certain nor immediate"*.[17]

b. Margin squeeze as abuse of dominant position

Regarding the most crucial issue of the complaint, the Court said that in order for the Commission to find an abuse of a dominant position in the form of a margin squeeze, it ought not to have established that Telefónica had a dominant position on both the wholesale market and the retail market[18] but only to the relevant wholesale markets. The existence of a dominant position derives in general from a combination of several factors. Among those factors figure the existence of large market shares[19] and the freedom of action.[20] A market share of 50 % constitutes in itself, save in exceptional circumstances, a dominant position.[21] Likewise, a market share of 70 to 80 % is, in itself, a clear indication of the existence of a dominant position[22] (Telefónica was found to hold a market share of 84 %).

The Court also pointed out that Article 82 EC refers to conduct which is liable to influence the structure of the market where, precisely because of the presence of the undertaking concerned, the degree of competition is already weakened and which, through recourse to methods different from those governing normal competition in products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing on the market or the growth of that competition.[23]

Contrary to the applicants' contention, the Commission did not analyse the margin squeeze as a *de facto* refusal to contract but as the resulting obligations. A margin squeeze is the result of the spread between the prices for wholesale services and those for retail services and not of the level of those prices as such. In particular, that squeeze may be the result not only of an abnormally low price on the retail market, but also of an abnormally high price on the wholesale market (see, to that effect, *TeliaSonera*, paragraphs 97 and 98).

Accordingly, the Commission was not required to demonstrate that Telefónica charged excessive prices for its wholesale indirect access products or

15 Guidance on the Commission's enforcement priorities in applying Article 82 (102 TFEU), of the EC Treaty to abusive exclusionary conduct by dominant undertakings (COM 2009, Brussels, 9 February 2009, OJ 2009 C 45/7).

16 See Case 322/81 *Nederlandsche Banden-Industrie-Michelin* v *Commission* [1983] ECR 3461; Case C-202/07 P *France Télécom* v *Commission* [2009] ECR I-2369 and T-301/04 *Clearstream* v *Commission* [2009] ECR II-03155.

17 See point 121 of the Decision.

18 Case C-52/09 *TeliaSonera* (n. 4).

19 Case T-30/89 *Hilti* v *Commission* [1991] ECR II-1439 and Case T-66/01 *Imperial Chemical Industries* v *Commission* [2010] ECR II-2631.

20 Case 85/76 *Hoffmann-La Roche* v *Commission* [1979] ECR 00461; T 65/98 *Van den Bergh Foods* v *Commission* [2003] ECR II-04653 and *Imperial Chemical Industries* v *Commission* (n. 18), see also *France Télécom* v *Commission* (n. 15).

21 Case C-62/86 *AKZO* v *Commission* [1991] ECR I-3359 and *Imperial Chemical Industries* v *Commission* (n. 18).

22 Case T-30/89 *Hilti* v *Commission*; Joined Cases T-191/98, T-212/98 to T-214/98 *Atlantic Container Line and Others* v *Commission* [2003] ECR II-3275.

23 *Hoffmann-La Roche* v *Commission* (n. 19), paragraph 76 above, paragraph 91; *Nederlandsche Banden-Industrie-Michelin* v *Commission* (n. 15), *France Télécom* v *Commission* (n. 15), and *Deutsche Telekom* v *Commission* (n. 3).

predatory prices for its retail products.[24] In order to assess the lawfulness of the pricing policy applied by a dominant undertaking, reference should be made, in principle, to pricing criteria based on the costs incurred by the dominant undertaking itself and on its strategy.[25]

So the appropriate test for establishing the margin squeeze consisted in determining whether a competitor having the same cost structure as that of the downstream activity of the vertically integrated undertaking would be in a position to offer downstream services without incurring a loss if that vertically integrated undertaking had to pay the upstream access price charged to its competitors, by reference to the costs incurred by Telefónica without undertaking a study of the margins of the main alternative operators on the Spanish market. The 'ladder of investments' theory does not require that all levels be accessible should be rejected as the process that enables alternative operators to invest gradually in their own infrastructure can constitute a viable strategy only where there is no margin squeeze practice at the different levels of the ladder.

c. Effects of Telefónica's conduct on national competition

A system of undistorted competition, as laid down in the Treaty, can be guaranteed only if equality of opportunity is secured between the various economic operators. Equality of opportunity means that Telefónica and its at least equally efficient competitors are placed on an equal footing on the retail market. The Commission did not make a manifest error of assessment when it considered that the dominant undertaking's downstream activity must be profitable over a period corresponding to the lifetime of its assets.

Telefónica had underestimated the LRAIC, since it had included only the incentives and commissions granted to the sales network for each new subscriber, excluding any cost relating to the company's marketing structure. As is clear, the long-run incremental costs of a product corresponds to the product-specific costs borne by the firm in the long term associated with total production of the product and, accordingly, to the costs that the undertaking would have avoided in the long term if it had decided not to produce that product. The Commission thus observed that the long-run incremental cost must include not only all the fixed and variable costs directly associated with the production of the product concerned, but also a proportion of the common costs associated with that activity.

For the purposes of establishing an infringement of Article 82 EC, it is sufficient to show that the abusive conduct of the undertaking in a dominant position tends to restrict competition or, in other words, that the conduct is capable of having, or likely to have, that effect.[26] The pricing practice concerned must have an anti-competitive effect on the market, but the effect does not necessarily have to be concrete, and it is sufficient to demonstrate that there is a potential anti-competitive effect that may exclude competitors who are at least as efficient as the dominant undertaking (*TeliaSonera*).

It also follows from the case-law of the ECJ that, in order to determine whether the dominant undertaking has abused its position by the pricing practices it applies, it is necessary to consider all the circumstances and to investigate whether the practice tends to remove or restrict the buyer's freedom to choose his sources of supply, to bar competitors from access to the market, to apply dissimilar conditions to equivalent transactions with other trading partners, thereby placing them at a competitive disadvantage, or to strengthen the dominant position by distorting competition.

d. Lack of subsidiarity, proportionality and legal certainty

Finally, the Court observed that assuming that the Commission were able to use Article 82 EC for regulatory purposes, *quod non*, its intervention in the present case would run counter to the principles of subsidiarity, proportionality and legal certainty, since it interferes without good reason in the exercise of the powers of the CMT.

It follows that *"the decisions adopted by the NRAs on the basis of the 2002 regulatory framework do not deprive the Commission of its powers to take action at a later stage in order to apply Article 82 EC by virtue of Regulation No 17 and, since 1 May 2004, Regulation No 1/2003"*.[27]

24 See, to that effect, *Deutsche Telekom* v *Commission* (n. 3).

25 See *Deutsche Telekom* v *Commission* (n. 3) and *TeliaSonera* (n. 4).

26 Case T-203/01 *Michelin v Commission* [2003] ECR II-4071, Case T-219/99 *British Airways v Commission* [2003] ECR II-5917 and Case T-201/04 *Microsoft v Commission* [2007] ECR II-03601.

27 Point 300 of the Decision.

The Court insists on separating the regulatory function from the competition authority, stating that the CMT as a regulatory authority and not a competition authority has never intervened to enforce Article 82 EC or adopted decisions relating to the practices penalised in the contested decision (recitals 678 and 683 to the contested decision). Even on the assumption that the CMT were required to consider whether Telefónica's practices were compatible with Article 82 EC, the Commission would not thereby be precluded from finding that Telefónica was responsible for an infringement. The Commission thus cannot be bound by a decision taken by a national authority pursuant to Article 82 EC.

Furthermore, it must be borne in mind, so far as concerns the relationships formed in the context of proceedings conducted by the Commission pursuant to Articles 81 EC and 82 EC, that the rules for the implementation of the duty of sincere cooperation which stems from Article 10 EC and which binds the Commission in its relationships with the Member States have been stated in, *inter alia*, Articles 11 to 16 of Regulation No 1/2003, in Chapter IV headed 'Cooperation'. Those provisions do not expressly require the Commission to consult the NRAs.

4. Comments on the decision

The e-communications networks have been recognized as a major contributor to both the national and the EU economy. This is reflected in the Commission's continuous effort to lift any barriers to competition. The same policy has concluded to some major regulations regarding wholesale pricing and market definition after 2 decades of liberalizing and harmonizing the national markets. Strict sliding paths have been applied to interconnection tariffs and an effective network cost analysis have contributed to a broader market with easier access to the incumbents network, many innovative services, adequate competition in the relevant markets and, of course, more benefits for the consumers and the related technology. The contested decision is a part of a long-run series of Commission relevant market analysis, in cooperation with the local NRAs, the outcome of which was the issuance of decisions against regional incumbents for market distortions, particularly through pricing.

Giving that the total of the competitive wholesale access products depend on the local loops of the incumbent, the access and availability to this essential facility depends not only on the available unbundled local loops but also on the generic financial terms on which these products are offered. It is clear that in controlling any abuse of a dominant position on the market, in so far as trade between Member States is capable of being affected, Article 82 EC refers to conduct which is liable to influence the structure of the market where, precisely because of the presence of the undertaking concerned, the degree of competition is already weakened and which, through recourse to methods different from those governing normal competition in products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing on the market or the growth of that competition.[28]

So, practically, what the Court said in this case is that the competition authorities, when searching for margin squeeze practice on a network pricing, first need to identify the market(s) affected, then to examine any abusive dominant position and, lastly, to measure whether an REO (Reasonably Efficient Operator) will be able to efficiently compete with the prices offered by the incumbent. On that course the Court have repeatedly cited the landmark decisions of *Deutche Telekom vs Commission* and *TeliaSonera*, which have set new rules on the quest of which behavior hides a price abuse and have settled that margin squeeze is a separate price abusive practice, regardless of whether it is accompanied with an unreasonable gap between wholesale and retail pricing.[29]

No doubt that margin squeeze may lead to serious distortions on liberalized network markets and has led to the provision of a number of *ex-ante* regulation that should work in addition to the ex-post examination of each case. It has been cleared that accounting separation[30] is an effective method to avoid cross subsidization and may control the effects of discriminatory pricing. But still the problems exist even in

28 *Hoffmann-La Roche v Commission* (n. 19), para 91; *Nederlandsche Banden-Industrie-Michelin v Commission* (n. 15) para 70; *France Télécom v Commission* (n. 15); *Deutsche Telekom v Commission* (n. 3).

29 Press release: "Digital Agenda - Commission tells German telecoms regulator to amend or withdraw fixed termination rates plan", IP/13/766 <*http://europa.eu/rapid/press-release_IP-13-766_en.htm*> *accessed 18.09.2013*.

30 Directive 2002/21/EC, Commission Recommendation of 19 September 2005 on accounting separation and cost accounting systems under the regulatory framework for electronic communications, Recommendation 98/322/EC.

the markets where the local NRA has applied all possible *ex-ante* regulation, as the relevant EU case law shows. That is why a functional separation obligation is also implemented (as an option) into the last EU telecommunications framework package, though still no NRA has enacted it in any of the EU markets.

Telefónica complained for lack of legal certainty when it comes to examine margin squeeze and regulated prices. The argument seems to be based on the fact that the accepted profit margin for each market is something to be examined case by case and thus provides no legal certainty because it is subjective. *"The need, though, to an undertaking to have legal certainty in order to promote innovation and investment is acknowledged in recital 38 of Regulation 1/2003"*.[31] The Court responded that Telefónica had a lot of discretion to follow the legal instruments set by the regulatory framework and use it in its pricing policy and increase its retail prices. In my personal opinion, the Court could have dealt a bit more with the fact that we cannot yet talk for a single and fully-harmonized European market, so each member's economy is different.

Thus, a margin squeeze must be always seen by taking into account the dynamics of each particular economy and not just a pre-set comparison between the wholesale upstream and the downstream competitors. Following the particular details of each market is more, let's say, fair since excessive marketing expenses and subsidy of terminals may distort this ratio without indeed establishing an abusive margin squeeze by the dominant operator. Examining each regional market separately gives a better outcome on how competitive it is and, in parallel, allows enough space for innovation. *"Dynamic and innovative markets feature dynamic pricing strategies in which prices can rationally diverge significantly from unit variable cost. Thus skimming pricing can involve initial high prices; more significantly, and widespread in many markets, penetration pricing involves very low initial prices, often below marginal cost. Such policies impact on prices, margins, and sales volumes over time, and hence complicate any assessment of market power. It can also be argued that any attempt to squeeze profit in such industries will damage the incentive to invent, which is the lifeblood for dynamic competition."*[32]

A Greek Administrative Appellate Court draw a unprecedented strict line stating, in a relevant case of the Greek incumbent (OTE) versus the Greek NRA (EETT), that *"even the existence of a margin squeeze practice suffices for proving an abusive pricing policy and no need for further examination of possible anti-competitive behavior exists."*[33] Given the fact that the Greek telecoms market literally lost almost all fixed alternative operators within a period of 8 years, such a general rule should apparently have been applied earlier!

Furthermore the Court re-affirmed its settled view that the application of the competition law is not prohibited by the application of sectoral regulation that can be distorted or limited by any stakeholder.[34] So the fact that a dominant operator is fully compliant with the regulatory framework does not mean that it does not (intentionally or not) abuse its dominant position.

What this case reaffirms is that so many years of applying *ex-ante* regulation on (often over-regulated) e-communications markets, *ex-post* examination still reveals a kind of non-quite adequate regulatory framework. The market seems a bit trapped in a vicious circle: *ex-ante* regulation is never enough and *ex-post* examination is not so effective. This has led to an increasing need for *de facto* pricing regulation. As those services become essential, we see a stronger need for centrally implied price controls.[35] Towards a single European market, the Commission (with the NRAs) has given a lot of effort to regulate tariffs, as it seems the only way for an effective competition. This may mean that the "hypothetical monopoly test" is no longer sufficient to measure pricing abuses and market boundaries.

It seems that the advent of new type of networks, the Next Generation Networks (NGNs), modifies the competitive environment in a number of markets, in particular regarding LLU and wholesale broadband access. However, according to the Commission, *"as*

31 R. Whish, D. Bailey *Competition Law*, Oxford University Press, 7th Edition 2012 p. 261. See also comments in p. 119 on "object restrictions" as a mean for legal certainty citing opinion of Advocate General Kokott in *T-Mobile* case (C-8/08).

32 Ian M. Dobbs "The Assessment of Market Power and Market Boundaries Using the Hypothetical Monopoly Test", Department of Accounting and Finance and Newcastle School of Management, University of Newcastle upon Tyne, 2002, note 9.

33 Case no 2193/2009, *DiMEE* (Media and Communications Law Review) 4/2009, p. 567 (see also the contested decision of the NRA (EETT) 447/01/26.07/2007 on DiMEE 2007, p. 441 commented by Spiros Tassis).

34 C-359/1995 P and C-379/1995 P, *Commission and France v Ladbroke Racing* [1997] ECR I-6265.

35 See also Case T-201/04*Microsoft* and the "fair pricing for the software interoperability".

long as competitive conditions have not changed, the move to NGNs does not provide an opportunity to roll back regulation on existing services".[36] Further, *"planned changes in the access network may potentially make it more difficult to continue to carry forward regulated remedies such as local loop unbundling (at established access points), that are designed to address the lack of effective competition in the provision of broadband services".*[37] It remains to be seen how those changes will push for a totally new access regulation. For a start it seems that we are heading to a single telecoms European regulator.[38]

Telefónica, S. A. and Telefónica de Espana, S.A.U appealed to the ECJ (C-295/12) on the grounds that the General Court committed several errors of law.

36 European Commission, Explanatory note, SEC(2007) 1483 final (see note 2), p. 164.

37 Ibid. p. 164.

38 *"The European Commission is thought to be considering a plan for a single telecoms regulator to cover all 28 member states" <http://www.bbc.co.uk/news/business-23695623> accessed 19.09.2013.*