COOPERATION AGREEMENTS (TELECOMMUNICATIONS): THE CEGETEL CASE

Subject: Cooperation agreements
Joint ventures
Product market
Geographic market
Market shares
Ancillary restrictions
Exclusive distribution
Exclusive supply
Non-competition clauses

Industry: Telecommunications
(Some implications for other industries)

Parties: Cégétal SA
Société Nationale des Chemins de Fer Français
Télécom Développement

Source: Commission Decision, dated 27 July 1999, published in the Official Journal, L.218, dated 18 August 1999

(Note. In one respect this is rather a peculiar case, in that the party providing a substantial telecommunications infrastructure is not itself in the telecommunications business. It runs a railway, but happens to have the infrastructure as part of its internal requirements. The opportunity for a new operator in the telecommunications sector to make use of this infrastructure must have been irresistible. It was also attractive to the Commission, which saw the agreement concluded between the new entrant and the railway company as a wonderful opportunity to challenge the dominance of the market by France Telecom, without distorting competition. The Commission recognised the ways in which the cooperation agreements between Cegetel and SNCF may technically have restricted competition but concluded that there was nothing in them to justify action under Article 81(1). There is plenty of potential competition: a number of telecommunications operators are building or have announced plans to build national fibre optic networks in France.

Most of the restrictions in the notified agreements were ancillary to the operation of the joint venture and necessary to ensure its entry into the market. Technical needs justify the exclusive use by the joint venture of SNCF's optical fibre network. It is not unreasonable for the joint venture to have priority use of SNCF land, given that other operators are not excluded from using it as well. Exclusive distribution by Cegetel of the joint venture's voice telephony services ensures that the joint venture will have a sufficient demand for its services to

sustain its entry into the market. Exclusive supply of the joint venture's services to Cegetel ensures that the joint venture has an effective and profitable minimum volume of activities. The non-competition clauses guarantee that Cegetel and SNCF, "two non-competitors who have entered a product market which is new to both of them", will concentrate their efforts on the joint venture. These points in the Commission's decision are strained to their limits, but are probably justified in the overall assessment of the competitive position. Four critical comments were received from interested parties but did not change the Commission's views.)

1 The Facts

A Introduction

(1) On 11 April 1997 Cegetel SA (Cegetel), a new telecommunications operator in France, and Societe nationale des chemins de fer francais (SNCF), the French national railway company, concluded a number of agreements, under which they will cooperate through a jointly-owned subsidiary, Telecom Developpement (TD), to develop and run a national long-distance telecommunications network along the French national railway network.

(2) The notified transaction is linked to the creation of Cegetel. By its decision of 20 May 1999, the Commission declared that the agreements setting up Cegetel as a telecommunications operator in France did not give grounds for objection under Article 81(1) of the EC Treaty.

B The Parties

(3) SNCF is the state-owned railways operator in France, with both industrial and commercial activities, providing transport services on the nationwide rail network. Its core activities are passenger and freight transport, and related and complementary activities. SNCF has its own telecommunications network to satisfy its own needs. The aggregate turnover of SNCF for 1997 was € 6,573m.

(4) Cegetel is a telecommunications operator, created in 1996, owned by the French water utility company Vivendi SA (previously known as Compagnie Generale des Eaux (CGE)), British Telecommunications plc (BT), Mannesmann AG and indirectly by SBC International Inc. Since 1 February 1998, Cegetel has offered a full range of telecommunications services to all the different segments of the French market. Cegetel also operates a nationwide GSM network through its subsidiary Societe francaise de radiotelephonie (SER). The aggregate turnover of the Cegetel group in 1997 was approximately € 1,610m.

(5) TD is a private company with limited liability incorporated under French law, created in 1996 by SNCF in which, by virtue of the notified agreements, Cegetel becomes a shareholder.

C Transaction

(6) The notification relates to the Framework Agreement dated 11 April 1997, the purpose of which is to define the principles governing the relations between SNCF and Cegetel both with respect to the shareholding of Cegetel in TD and as regards the modalities of deployment of the network and operation of telecommunications services.

(7) The aim of TD is to develop and run a national, long distance telecommunications network based on:

(a) the surplus transmission capacity on the existing SNCF telecommunications network;

(b) the optical fibre cables made available to it by Cegetel or its subsidiaries; and

(c) additional investment for using its own cables as part of an installation plan laid down in the agreements for the initial period 1997-2000.

(8) TD holds a licence to operate long-distance, public access networks. The notified agreements provide also for TD to develop and deploy a long-distance telecommunications service in France capable of constituting an alternative to the offer of the incumbent operator.

(9) On the basis of this network, owned by TD, Cegetel intends to become the second full service telecommunications operator in France by offering a complete range of telecommunication services including voice telephony between fixed points and transmission capacity for other operators.

(10) TD will not provide a connection service for end-users, namely businesses or individuals, except for the connections required by SNCF. Under Article 1 of the frame-work agreement, TD will provide:

(a) a long-distance interconnection service for telecommunications operators:

(b) long-distance transmission capacities for Cegetel and Cegetel subsidiaries but also for other network operators and telecommunications services providers;

(c) an end-to-end, long-distance voice telephony service, which is to be distributed exclusively by Cegetel's subsidiaries, Cegetel Le 7 (previously known as Telecom Developpement Services (TDS)) (residential market) and Cegetel Entreprise (businesses), jointly owned with TD.

(11) As a result of the clauses on the acquisition of an interest in the share

capital of TD by Cegetel the capital share of TD will be divided up as follows:

SNCF:	between slightly more than 50% and 60%,
Cegetel:	between 40% and slightly less than 50%,
third party (if any):	10%.

(12) TD is governed by a management board (the *Directoire*), a supervisory board and a shareholders' committee. The management board, which is entrusted with the day-to-day business of TD, is composed of five members, two appointed on a proposal from SNCF, two on a proposal from Cegetel, and a qualified person unconnected with either of the Parties (the president) appointed by the supervisory board, by joint agreement between the Parties. The supervisory board exercises supervision over the management board's conduct of business and is made up of an odd number of members. The number of members appointed by the shareholders meeting on proposal by SNCF will always be greater by one member than the number of members appointed by Cegetel. The president of the supervisory board will be one of the members chosen by the members of the supervisory board appointed on a proposal from SNCF. The shareholders committee, made up of 10 members, half appointed by Cegetel and half by SNCF, is set up to determine the joint position of the Parties on a number of issues, including the strategic decisions and orientation of TD, the adoption and modification of the business plan and annual budget and acquisitions of assets or realisation of important investments.

D Relevant Market

(a) Product market

(13) TD acts as an operator of a telecommunications network alternative to the network of the incumbent operator, France Telecom. It will provide; mainly for Cegetel but also for other operators, transmission capacity for national, long-distance telecommunications traffic and, on an exclusive basis for Cegetel, long-distance, voice-telephony services. The notified agreements will therefore address:

(i) the market for carrier's carrier services and

(ii) the market for the provision of fixed, long-distance telecommunications services. These two markets have been defined in a number of previous Commission decisions (such as *Phoenix/Global*, 1996, and *Unisource*, 1997). As in past decisions, moreover, the precise product market delimitation in this case can be left open since, even on the narrowest possible definitions, the proposed transaction does not give rise to competition problems.

(b) Geographic market

(14) The scope of the geographic market in telecommunications is

determined:

(I) by the extent and the coverage of the network and the customers that can economically be reached and whose demand may be met and
(ii) by the legal and regulatory system in force in the territory where the operator is active.

(15) Having regard to the licensing and regulatory framework for the provision of fixed, long-distance telecommunications services, the geographic market for these services must be regarded as being national in scope. Furthermore, the TD network will be limited to the territory of France. Accordingly, the relevant geographic market for the provision of carrier's carrier services is France.

(c) Situation of the parties on the telecommunications market

(16) SNCF is not commercially active in the telecommunications sector. TD and Cegetel entered the long-distance, voice-telephony market (deregulated in France on 1 January 1998) only on 1 February 1998. In 1997, TD had had a negligible share of the transmission capacity supply market.

(d) Main competitors

(17) Until 31 December 1997, France Telecom had a monopoly on the long-distance voice-telephony market in Prance, and it still has a significant market power on that market. Similarly, France Telecom has a very strong position on the markets for long-distance, transmission capacity supply and for the provision of interconnection services, with a market share exceeding 95% in both of them.

(18) Many companies have entered or intend to enter the French telecommunications market, either as full service telecommunication operators (9 Telecom) or on specific market segments: resale of voice-telephony services (Axis, Kertel, and others), telecommunications networks (Hermes, Colt, Esprit Telecom), services for corporate clients (WorldCom, Siris, Colt, Omnicom, and others), or local access (Lyonnaise Cable), and so on. As of 8 April 1999, 59 licences had already been delivered for telecommunications network and/or services provision by the national telecommunications regulator. Seven operators had been granted a short prefix for carrier pre-selection.

E The Notified Agreements

Agreements

(19) The principles and detailed rules for the collaboration between the Parties have been defined in the Agreement between SNCF and Cegetel for their partnership within the company Telecom Developpement. This agreement (the framework agreement), signed on 11 April 1997, includes:

- a deployment plan for the TD network (Annex 2 to the framework agreement),
- an initial business plan relating to the development of TD (Annex 9 to the framework agreement),
- a marketing agreement aimed at organising the conditions of the distribution by Cegetel of the long-distance telephone services of TD), the supply of an interconnection service and the supply of long-distance transmission capacity (Annex 3 to the framework agreement),
- a contract relating to the deployment by SNCF of the TD network (Annex 5 to the framework agreement),
- a contract relating to the maintenance by SNCF of the TD network (Annex 6 to the framework agreement).

Contractual provisions

(a) *Contribution to TD of existing optical fibre network capacity*

(20) In an agreement concluded on 22 November 1996, SNCF contributed to TD exclusive rights for the use of the surplus capacity on its existing optical fibre network. Furthermore, Cegetel transferred its own long-distance optical fibre network and those of its subsidiaries to TD. Cegetel Longue Distance was taken over by TD.

(b) Priority use of railway land

(21) In an agreement concluded on 22 November 1996, SNCF granted TD a non-exclusive right to occupy public railway land for a period of 30 years, to allow it to deploy a telecommunications network. In order to enable TD to complete the installation of its network in the shortest possible time, SNCF has also granted it a priority right of access to SNCF's land, guaranteed by a penalty clause applicable for a period of three and a half years, from 1997 to 2000.

(22) The precise details regarding the scope of this priority access and the arrangements for its application were amended following intervention by the Commission, as is described in recitals 28, 29 and 30.

(c) Exclusive distribution of voice-telephony services

(23) A joint company between Cegetel and TD, Cegetel Le 7, in which Cegetel has an 80% stake and TD a 20% stake, will be solely responsible for marketing TD's long-distance telephony services for the general public. Similarly, end-to-end, voice-telephony services for corporate clients will be exclusively distributed by Cegetel Entreprise, also owned 80% / 20 % by Cegetel and TD.

(d) Exclusive supply of transmission capacity

(24) Cegetel has signed an exclusive supply agreement with TD, on behalf of both itself and its subsidiaries, under the terms of which they undertake that TD is their sole supplier for the provision of transmission capacity for long-distance telecommunications traffic in France. However, Cegetel is permitted to use other suppliers if TD's prices should at any time prove to be above the market price. In addition, TD may buy capacity from other operators to meet Cegetel's requirements. In addition, Cegetel is bound by its previous supply agreements.

(e) Non-competition

(25) SNCF has undertaken not to engage, either directly or indirectly via a subsidiary, in any activity in the telecommunications field that would be in competition with TD or the Cegetel group.

(26) Cegetel has promised to abstain from any investments in long-distance telecommunications networks, apart from its investment in TD.

(27) TD has undertaken not to compete with Cegetel Le 7 and Cegetel Entreprises as regards the marketing of telecommunications services.

F Contractual Changes

(28) On 18 March 1998, the Commission informed the parties that it considered the clause governing the priority use of railway premises by TD as falling within the scope of Article 81(1) of the EC Treaty and that, as it stood, it was not eligible for an exemption under Article 81(3). On 20 April 1998, the parties proposed amending the clause in question in order to clarify the scope and practical application of the priority access granted to TD, and thus to spell out clearly the conditions under which the penalties provided for in the agreements would be applicable. Taking into account the Commission's observations, the parties introduced on 31 July 1998 an amendment to the original agreements under which they make provision for:

(i) equal treatment for third parties in those exceptional cases where the railway infrastructures in question are the only means of putting in its cables (narrow valley structures); and

(ii) that SNCF (or, where appropriate, Reseau Ferre de France) remain free to give access to the railway infrastructures to other telecommunications operators, provided that this can be done without interfering with the development of TD's network.

(29) These amendments allow SNCF to give access to its infrastructures to other operators, provided that this can be done without interfering with the development of TD's own network.

(30) Furthermore, the priority right is limited to the minimum period required to implement the network (1997-2000), and there is an explicit undertaking that the priority rights shall not apply in the event of other companies' seeking access to specific portions of railway-owned land if the installation of cables on these sites is the only way of creating a telecommunications network.

C Third Party Observations

(31) Following the publication pursuant to Article 19(3) of Regulation 17, comments were received from four interested parties. The comments focused, in particular, on the changes submitted by the Parties regarding the priority use of railway land by TD, the conditional access to the railway premises under the agreement during the period of deployment of TD's network and to the alternatives to the rail network infrastructures in France for the purposes of installation of telecommunication networks. These comments were fully assessed by the Commission but proved not to be such as to cause the Commission to change its favourable position in the light of the contractual changes agreed by the Parties.

II Legal Assessment

A Application of Article 81(1) to the entry of Cegetel into capital share of TD

(32) SNCF and Cegetel are neither actual nor potential competitors. They operate on completely different markets. Cegetel is present, or emerging, on most segments of the telecommunications market in France, while SNCF, which is contributing the infrastructures on the basis of which the services will be developed and exploited, is not commercially active in the telecommunications sector. Moreover, neither SNCF nor Cegetel are present on the market for carriers' carrier services on which TD wilt mainly operate.

(33) SNCF is the state-owned railway operator and does not intend to become a telecommunications operator. TD was not created by SNCF in order to act as a telecommunications operator, but merely to deploy a telecommunications network previously used for its own internal needs. The French authorities have confirmed that the purpose of TD, as a subsidiary company of SNCF, is to be limited to the activity of exploiting that network (as confirmed by a letter of the French Secretary of State for Transport to the president of SNCF dated 17 July 1996). Through the notified agreement, Cegetel will be able to have access to the French nationwide railway infrastructures for the purpose of building up a telecommunications network of its own. In exchange, SNCF will receive an atypical financial return from its assets and will obtain telecommunications capacity for its own internal purposes.

(34) Furthermore, the deployment of a telecommunications network with national coverage takes a number of years and requires substantial investment. TD could not reasonably be expected to undertake such investments without the support of a full service telecommunications operator aiming to establish itself on the basis of infrastructure and services alternative to those provided by the incumbent operator in France.

(35) Cegetel is a new entrant in the French telecommunications markets facing strong competition from France Telecom. It does not have its own backbone network and has been, until now, dependent on the incumbent operator for the infrastructure by means of which it offers its services. By means of TD, Cegetel will be able to have access to the French nationwide railway infra- structures for the purpose of building up a telecommunications network of its own. This network will be the first nationwide alternative network (to the one controlled by the incumbent operator) to be put into service in France. Although for the purposes of creating telecommunications networks there are a number of alternative infrastructures to that of the railways, which Cegetel could in fact have studied before deciding to acquire an interest in TD, it is unlikely that without TD's existing network and the priority usage of the railway premises of SNCF, Cegetel could have been present on the long-distance, voice-telephony market (including switched transit or dedicated transit services) as early as 1 February 1998.

(36) The notified agreements provide for an allocation of tasks between, on the one hand, TD, which will be in charge of the technical aspects of the establishment, maintenance and operation of the telecommunications network, and, on the other hand, Cegetel, which through Cegetel Le 7 and Cegetel Entreprises will provide commercial telecommunication services to end-users.

(37) The French telecommunications market has only relatively recently been fully liberalised (1 January 1998) and new entrants are exposed to strong pressure from the incumbent operator which has traditionally represented the sole source of domestic transmission lines in that country. Liberalisation of alternative infrastructures occurred in France on 1 July 1996. A number of tele-communications operators are building or have announced plans to build national fibre optic networks in France, including Hermes (of which SNCF is an indirect shareholder through a 9% shareholding in HitTail BV), COLT, Worldcom / MCI and Cable & Wireless. Against that background, it does not appear that the notified agreement has the effect of preventing, restricting or distorting competition within the relevant market referred to above. By enabling Cegetel to build up its own network and offer long-distance services over the transmission capacity developed by TD, the agreements will allow that company to compete more effectively on the market by ending its dependency on the incumbent operator for its backbone network.

(38) The agreements are not likely to affect the competitive position of third parties, in so far as SNCF is not unduly precluded from granting access to its infrastructures to other operators. Furthermore, third-party operators would benefit from the existence of the additional transmission capacity for telecommunications services that TD will create.

(39) The Commission has itself recognised that new licensed operators such as TD required access to pathways across public and private property to enable them to roll out their networks, as well as acknowledging the merits of facility sharing in terms of town planning, and for environmental and economic reasons, albeit in an interconnection context (see Commission Directive 90/388/EEC of 28 June 1990, on competition in the markets for telecommunications services, as amended).

(40) In conclusion, on the basis of the arguments set out above, the acquisition of a shareholding by Cegetel in the share capital of TD falls outside the scope of Article 81(1) of the EC Treaty.

B Application of Article 81(1) to the Contractual Provisions

(41) On the basis of arguments developed below, the contractual provisions identified in recitals 28, 29 and 30 are ancillary to the activity of TD in as much as they are directly linked to, and necessary for, such activity. Given the financial investment required to deploy an alternative nationwide telecommunications network which constitutes the basis of the operation of Cegetel, itself a new entrant into the French telecommunications market, those provisions ensure TD the conditions of operation required to secure its entry into the market within a short period of time.

(a) Exclusive use by TD of the SNCF optical fibres

(42) By means of this provision, SNCF ensures that its venture TD will have the necessary resources for carrying on its main business. This is an exclusive right which concerns the very nature of the contribution agreement. This provision also arises from the SNCF's decision not to act as a telecommunications operator and to transfer to its subsidiary TD all the activities relating to the operation of the network built up on the railway facilities. Furthermore, the task of TD involves the configuration and maintenance of a nationwide telecommunications network starting from the optical fibres already deployed by SNCF. Those fibres require an upgrading in order to increase their capacity and ensure their integration into the network. The management, integration and upgrading of such network would be extremely difficult unless the exclusive use of all the fibres which constitute the network has been secured.

(b) Priority use of railway land

(43) The purpose of this provision is to secure for TD its means of operation by ensuring that the deployment of the telecommunications network will take place within the schedule contained in its business plan. Cegetel is relying solely on the long-distance network of TD for the transport of the long-distance telecommunications traffic. The priority use of railway land is justified in view of the conditions of deployment of the network imposed by the law and of the requirements of continuity of railroad transport operation and security of circulation of trains. The wording of the agreements, as amended by the Parties (see recitals 28, 29 and 30), does not imply that any exclusivity is given to TD and does not prevent third parties from having access to the railway land for the purposes of laying cables, and thus does not hinder the construction of networks by competing operators.

(c) Exclusive distribution of TD's voice-telephony services by Cegetel

(44) The commercialisation agreement provides that TD will not, by itself, market voice-telephony services to end-users, and will instead provide those services to Cegetel. The strategy agreed between the two parent companies results in TD being in charge of the technical aspects of the setting up and operation of the network; and Cegetel, through Cegetel Le 7 and Cegetel Entreprises, assumes the commercial operation of client services. This provision reflects SNCF's intention to limit the activity of TD to the operation and exploitation of the telecommunications network. As a result of that limitation, the commercialisation agreement ensures that TD will find a demand for its long-distance voice-telephony services which will be marketed by Cegetel. The agreement ensures therefore that TD will have sufficient demand for its services to sustain its entry into the market and contributes to its long-term viability as operator.

(d) Exclusive supply clause

(45) Similarly, the obligation contained in Articles 4(4) and (5) of the framework agreement, by requiring Cegetel to establish its operation on TD's network, ensures that the venture company has an effective and profitable minimum volume of activities, as well as regular profits. It should be recalled, however, that this undertaking is considerably reduced on the one hand by Cegetel's option of being supplied by a third party if the TD prices are less favourable than those on the market, and on the other hand by Cegetel's adherence to previous supply undertakings.

(46) On the basis of the particular circumstances of this case, it can be concluded that the exclusive *use* of the SNCF optical fibre cable network capacity, the priority use of railway land resulting from the amendments introduced by the parties on 31 July 1998, the exclusive distribution of voice-

telephony services and the exclusive supply clause are directly related and necessary to the successful implementation of the network and operation of TD. Hence, they have to be regarded as ancillary restraints to the project intended by the Parties under the competition rules of the EC Treaty.

(47) Ancillary restraints are to be assessed together with the creation of the company. In this respect, as the agreements between SNCF and Cegetel concerning TD have been found not to fall within the scope of Article 81(1) of the EC Treaty, it follows that the provisions detailed above do not do so either.

(e) Non-competition

(48) The non-compete terms applicable to SNCF (Articles 3 and 36 of the framework agreement) and to Cegetel (Article 4(8) of the framework agreement) guarantee that Cegetel and SNCF, two non-competitors who have entered a product market which is new to both of them, will concentrate their efforts on TD. Furthermore, given that the telecommunications network operated by TD, which is built upon the premises of French railway infrastructures, is essential for Cegetel's operation as a full telecommunications operator, those terms are necessary in order to ensure that TD becomes stable on the market. The non-compete obligation binding on TD ensures that TD will concentrate its efforts on the exploitation of the telecommunications network.

Article 1

On the basis of the facts in its possession, the Commission has no grounds for action under Article 81(1) of the EC Treaty and Article 53(1) of the EEA Agreement in respect of the notified agreements relating to the cooperation between Societe nationale des chemins de fer francais and Cegetel SA through their joint subsidiary Telecom Developpement.

Article 2

[...] □

Increase in the number of complaints to the Commission

In the last four full years the number of complaints to the competition in competition cases has continued to rise. In 1995, there were 114 complaints; in 1996, there were 159 complaints; in 1997, there were 177 complaints; and, in 1998, there were 192 complaints. The 1998 figure compares with 101 cases opened on the Commission's own initiative and 216 cases based on notifications.