ABUSE OF DOMINANT POSITION (TELECOMS): THE DT CASE

Subject: Abuse of dominant position
Pricing policy
Discrimination

Industry: Telecommunications

Parties: Deutsche Telekom AG

Source: Commission Statement IP/03/717, dated 21 May 2003

(Note. This is another instance of competition rules being called in aid to give new market entrants an opportunity to have access to an already established infrastructure. Yet competition rules alone are not enough to guarantee access: in the present case, the position is governed by legislation at both the European and the national levels. What the competition rules can do is to accelerate the process by which access is granted, since they can be used to challenge pricing policies based on a denial of access: see the second paragraph of the section below entitled "Background: Access to the local loop".)

The Commission has adopted a decision against Deutsche Telekom AG (DT) for abusing its dominant position through unfair prices for the provision of local access to its fixed telecommunications network (local loops). The Commission has found that DT charges new entrants higher fees for wholesale access to the local loop than the fees paid by DT's subscribers for fixed line subscriptions. This discourages new companies from entering the market and reduces the choice of suppliers of telecommunications services as well as price competition for consumers. The Commission's action stems from complaints by numerous new entrants in the German telecommunications market. In line with the gravity and duration of the abuse, the Commission levies a fine of €12.6 million.

According to the Commission, DT has been legally obliged since 1998 to provide competitors access to its local loops. In spite of this clear obligation, there still is very little effective unbundling of the local loops; and DT, with a market share of 95%, remains the dominant provider of broadband and narrowband retail access. Many new entrants have tried to compete with the incumbent operator. None of them has been able to reach significant market share, not least because DT charges competitors higher fees for local loop access than it charges its end users. As the Commission points out, this is clearly harmful to consumers, because competition between operators is the best means to bring the overall prices down. That is the reason for the Commission's action against unfair pricing by Deutsche Telekom and for its determination to be vigilant on any infringements of this kind.

The Commission had found that Deutsche Telekom was abusing its dominant position through unfair pricing. DT holds a dominant position on both the markets for both wholesale and retail access to the local loop. Regarding wholesale access, DT is the only German network operator having a network with nation-wide coverage. To provide a variety of services to end users, new entrants need access to this infrastructure on a wholesale basis. Regarding retail access, even after five years of competition, DT still has around 95% market share and the remaining 5% is divided among large numbers of DT's competitors.

Because of the insufficient spread between DT's local loop access prices and the downstream tariffs for retail subscriptions, new entrants have no scope for competing with DT for end consumers. The Commission's decision compares upstream access to the local loops with a bundle of different types of retail offerings, namely analogue, ISDN and ADSL connections. To achieve a coherent comparison, the Commission used a weighted approach taking into account the numbers of DT's retail customers for the different access types on retail level.

The Commission's assessment reveals, for the period 1998 through 2001, that DT charged competitors more for unbundled access at wholesale level than it charged its subscribers for access at the retail level. This constitutes a clear case of margin squeeze, because it leaves new entrants no margin to compete for downstream retail subscribers. As of 2002, prices for wholesale access were lower than retail subscription prices but the difference was still not sufficient to cover DT's own downstream product-specific costs for the supply of the end-user services. Even after the latest reduction of the wholesale prices by the German regulatory authority (RegTP), which became effective on 1 May 2003, this margin squeeze remains in place.

Fine

According to the Commission's Guidelines on the method of setting fines (Official Journal of the European Communities, C.9, 1998), the criteria for determining the amount of a fine are gravity and duration of the infringement, as well as aggravating or attenuating circumstances. The margin squeeze implemented by DT as an undertaking dominant both at the wholesale and retail levels constitutes a serious infringement. The result of this pricing strategy is that new competitors who need access to the local loops in Germany are seriously impeded. The relevant markets are markets of considerable economic importance. On the other hand, DT has steadily reduced the margin squeeze through tariff adjustments. Therefore the basic amount for gravity was set at €10 million.

The abuse was found to have lasted from 1.1.1998 until today: the infringement is therefore of long duration. The infringement was, however, less important in the period since 1.1.2002, due to the reduced scope for price adjustments under the

regulatory provisions in Germany. Therefore only the first four years until the end of 2001 account for an increase of the basic amount to €14 million. Finally, the Commission has reduced the fine to €12.6 million by assuming mitigating circumstances due to the fact that, under the sector specific regulation in Germany, there was some degree of legal uncertainty about the tariffs under scrutiny.

Background: Access to the local loop

The local loop is the physical circuit between the customer's premises and the telecommunications operator's local switch. Traditionally it takes the form of pairs of copper wires. New entrants on the telecommunications markets need access on fair and non-discriminatory terms to the local loops ("local loop unbundling") to be able to offer retail services to end-customers, as it would be impossible to replicate such a network built over a century.

Effective local loop unbundling is key for the spread of electronic communications services. It was imposed on the incumbent operators by way of legislation at EU level and, in some Member States, such as Germany, also at national level. However, local loop unbundling is not developing fast enough. The regulatory framework is not the only tool available. The conditions of local loop unbundling, such as pricing, are also subject to scrutiny under the EU competition rules.

In Germany, DT offers local loop access at two different levels. Besides the retail subscriptions to end customers, DT also offers unbundled access to the local loop to competitors, which allows them direct access to end-users. DT is thus active on the upstream market for wholesale local loop access to competitors and on the downstream market for retail access services to end-customers. Both markets are closely linked to each other.

DT's local access network is not the only technical infrastructure allowing for the provision of wholesale access services to competitors and of retail access services to end-users. But the other options, which include fibre-optic networks, wireless local loops, satellites, power lines, and upgraded cable TV networks, are not yet sufficiently developed and cannot be considered as equivalent to DT's local loop network.

According to the Commission's 8th Implementation Report of December 2002 (COM(2002) 695), two years after the EC Regulation on local loop unbundling came in force, only 1 million subscriber lines have been unbundled across Europe. The large majority of them (855,000) are in Germany, where unbundling had been mandated by national law in 1998; but even in Germany unbundled lines account for fewer than 5% of the total. ■