GETTING THE CHEMISTRY RIGHT FOR EU TELECOMS CONSOLIDATION

LESSONS FROM HUTCHISON / ORANGE
“Some operators claim that consolidation efforts should be allowed to achieve economies of scale and help [...] operators invest in the development and roll-out of new technologies”

“So far, [...] cross-European parent ownership has not helped to develop a Single Market [...] the regulatory environment is country-specific”

“When consolidation takes place within the boundaries of an already concentrated national market, we should be careful about the potential harm to consumers in that country”

“I can also think of other ways than mergers to promote efficiency gains among operators, such as network-sharing agreements.”

Joaquin Almunia, Vice President of the European Commission responsible for Competition Policy
MIXING THE ELEMENTS

- Pan-European vs national markets
- Efficiencies
- Technology innovation
- Merger control
- Sector Regulation

Consolidation
There have been three waves of consolidation in EU telecoms, driven by:

- Regulatory changes
- Technology innovation and
- Economies of scale.

Purely cross-border mergers have tended to attract less scrutiny because of the lack of horizontal overlaps. Although vertical overlaps were investigated (i.e. the reciprocal provision of access and interconnection between networks in different countries), such overlaps are less likely to raise issues if efficiencies can be demonstrated.

**Bottom line:** As of 2012, a fourth wave of consolidation seems to be emerging. However, the scope for further cross-border deals is limited going forward. We are more likely to see in-market consolidation of the *Hutchison / Orange* type.
The case was a 4 to 3 merger between the two smallest in-market players. The two remaining competitors are the incumbent Telecom Austria and T-Mobile Austria. Virtual mobile network operators without a full own network – the so-called MVNOs – practically do not exist in Austria today.

The Commission expressed serious doubts and opened an in-depth investigation, although the merged entity’s combined market share would be lower than its remaining competitors and within the safe harbour of the Commission’s own Horizontal Mergers Guidelines.

To get the deal through, the Commission insisted on the following remedies, although DG Connect had publicly said that just an access obligation would have been sufficient:

- Spectrum divestiture;
- Wholesale access obligation;
- Up-front MVNO new entrant.

On the basis of the limited publicly information available (the full text of the decision has not yet been published), we think this case confirms some old and emerging trends:

- First, the Commission’s assessment nowadays relies less on market shares and more on other factors, namely:
  - closeness of competition (e.g. the merging parties’ subscribers tend to switch between the two parties more often than they do with the other two MNOs);
IN-MARKET MERGERS
LESSONS FROM Hutchison / Orange (2)

- accumulation of spectrum in contiguous high value bands such as 4G (e.g. the merged entity would have a higher combined amount of spectrum in the 2.6 GHz paired frequency band than each of the other two remaining MNOs).

• Second, the Commission continues to seek the implementation of regulatory goals by way of conditions imposed under merger control rules.

• Third, the assumption that you need 4 MNOs to preserve retail mobile competition remains somewhat a “dogma” for the Commission, especially if you compare the situation with countries where there are fewer MNOs and more MVNOs (e.g., in KPN/Telfort, the Dutch NCA allowed a 4 to 3 merger with the incumbent MNO).

• Fourth, the Commission tends to consider with suspicion potential constraints on the merged entity resulting from technology innovation (such as the constraints Wi-Max could impose on 4G).

• Fifth, inconsistencies in EC policies regarding assessment of efficiencies – economies of scale are fully taken into account when deciding whether to impose sector specific regulatory conditions (e.g. in relation to mobile termination tariffs). However, there is little in the way of precedent on the assessment of the same efficiencies under EU merger control rules.

• Sixth, the Commission gives little weight to potential remedial action under sector regulation.

• Bottom line: in-market consolidation in the EU will likely continue to be allowed with strings attached to it, with a preference for structural remedies that promote infrastructure competition over service competition.
A recent EU sponsored study shows that the annual gains which would result from the building of a fully-fledged internal market amount to up to 0.9% of GDP, or up to 110 billion Euros, per year. These gains could be achieved by means of easier entries on more competitive markets and through a better exploitation of economies of scale, i.e. consolidation.

**Main obstacles:**

- lack of EU standards for interoperability
- National orientation of regulation
- heterogeneity in the implementation of EU telecoms rules

In the face of these findings, the Commission will publicly engage in 2013 with stakeholders on the ways to move forward. It is unclear what this may entail. The financial press reported this might include the promotion of network sharing.

“We’re working on a range of measures to create common and stable conditions across the EU for telecoms competition, investment and growth, which should also make cross-border consolidation more attractive,” said Ms Kroes.

“Various forms of asset sharing can promote competition and investment”
Network sharing is encouraged under EU sector specific rules and is normally regarded as pro-competitive under EU competition rules as long as it is limited to the Node B and RNC and excludes core network elements, such as frequencies and customer information.

This type of cooperation is commercially more fluid but does not guarantee the same level of legal uncertainty than concentrations would under merger control rules, because the parties must self assess the compatibility of their cooperation under the stricter legal test of EU anti-cartel law. Recent cases illustrate the inherent dangers of such self-assessment (e.g. Telefonica and Telecom Portugal have been fined almost 80 million euro together as the Commission decided their cooperation constituted a market sharing agreement in violation of EU anti-cartel law).

What's next? The idea of a pan-European network emerged at a private meeting between EU competition chief Joaquín Almunia and the leaders of Europe's biggest telecoms groups, including Deutsche Telekom, France Telecom, Telecom Italia and Telefonica, according to recent press reports. Perhaps the publication of EU guidelines on the assessment of network sharing would help achieve more legal certainty, thus promoting investment.
CONCLUDING REMARKS

Cross-border consolidation is seen more favourably but in practice it has less potential going forward.

In-market consolidation is still possible, as long as parties are prepared to offer both behavioural and structural remedies to preserve customers’ ability to switch and avoid accumulation of too much spectrum in contiguous and high value bands – e.g. 4G frequencies.

Other forms of consolidation may attract less scrutiny and create efficiencies – e.g. network sharing – as long as parties can create a structure that is “commercially fluid” but “competition law solid”.

There is an opportunity for trying to influence and shape regulatory policy in 2013 – key is to address both DG Competition and DG Connect.
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Bernard Amory practices competition law representing clients before the European Commission, national courts, and competition authorities in Europe and the European Courts in Luxembourg. He also oversees Jones Day’s Antitrust & Competition Practice in Europe.

Bernard’s recent or ongoing representations relating to Article 101 (restrictive practices) include: the air cargo case and the One World Alliance for American Airlines, the vitamins case for Aventis, the marine hoses case for Parker Hannifin, the paper and forestry products and industrial bags cases for UPM, the bananas case for Dole, the credit card investigation for MasterCard, the O2/T-Mobile infrastructure sharing and national roaming case on behalf of O2, and the Apple iTunes pricing investigation.

Some of the leading merger cases in which Bernard has represented the notifying party include: BT/MCI and BT/AT&T, Total/Petrofina, Renault/Nissan, and Procter & Gamble/Gillette. He also acts for intervening parties and complainants in merger cases, such as for Warner Music Group in EMI/Sony and EMI/Universal, Apple in Sony/BMG, Tele Denmark in Telia/Telenor, and AT&T in MCI/WorldCom/Sprint.

He also has significant experience in Article 102 (abuses), including the roaming case on behalf of Telefonica-O2 and Microsoft on behalf of a third party and Dell in the Intel rebates case. His experience on state aid and state measures include the representation of BUPA in the risk equalization scheme in Ireland and work for Bouygues.

Bernard served as council member of the International Bar Association (SBL) and is on the advisory board of the European Competition Journal.

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Yvan Desmedt advises clients on competition law and regulatory matters across a range of sectors, particularly in the regulated industries of TMT, energy and transportation.

His competition law experience includes merger control at the EU and national levels as a notifying party or third-party opponent. Examples include assisting SAP in a number of acquisitions in enterprise application software and BT in various acquisitions in the telecommunications sector. He also acted for intervening parties and complainants in a number of transactions, including Universal/EMI and Oracle/Sun.

His antitrust experience includes the investigation of interchange fees on behalf of MasterCard, the U.K. roaming case, and the Vitamins cartel at the EU level, as well as various infringement proceedings conducted by the Belgian competition authorities, including those involving diamond producer De Beers. Yvan regularly advises on commercial agreements, including joint ventures, distribution, and licensing. He has advised trade associations, including the GSM Association and the Committee for Electronic Domestic Appliances (CECED), on compliance issues and horizontal cooperation.

Yvan also has significant litigation experience. He has represented a number of fixed and mobile operators against the incumbent in Belgium. Those proceedings have involved cases before the competition authorities, regulators, administrative courts, and civil courts. He has assisted telecom clients in various other matters such as frequency auctions, licensing issues, site-sharing, and access agreements.

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Alexandre’s experience involves abuse of dominant position/monopoly offense, cartel, merger, and state aid cases. He represented DoubleClick in its merger with Google and BT in its various mergers since 1995 (including MCI, AT&T, Infonet and Radianz). He obtained a favourable judgment in a €500 million damage claim for abuse of dominant position against Belgacom Mobile and the largest fine ever imposed on a dominant enterprise by the Competition Council. He represented Dole in the banana cartel case and Bouygues Telecom in several state aid cases against the French government. He also represents Toyota in all its competition law related European distribution matters.

Alexandre is vice chair of the Communications Committee of the International Bar Association. He received an award from the Belgian American Educational Foundation and is a winner of the 2012 Antitrust Writing Awards for the article “EU Court of Justice Provides Guidance on Abusive Margin Squeezes” written in collaboration with Serge Clerckx. He also is a regular speaker at conferences.

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Prior to joining Jones Day, Francesco gained in-house telecoms experience during his secondment to the regulatory departments of Orange (wireless telecoms) and MCI WorldCom, now Verizon Business (internet and global telecoms).

He is recognised as a leading telecoms and competition law practitioner and he won the International Bar Association Communications Law Committee Young Lawyers Award in 2009.

Francesco has written various articles on antitrust/competition law and regulatory issues, including the EU chapter of the American Bar Association Telecoms Antitrust Handbook and the UK chapter of International Telecoms Law.