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EC State Aid Rules on Broadband Deployment in Rural Areas

Implementation and Functioning in Sweden

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Summary

This thesis concerns EC State Aid Law regarding measures to promote broadband deployment in rural areas. The purpose is to examine whether Community Law allows Member States to grant State aid to projects with this objective, and, if so, under which circumstances the granted State aid is compatible with EC Law. The situation in Sweden is analysed, in relation to EU15.

Broadband access is a highlighted policy area of the European Union, because of its ability to enhance economic growth and social cohesion. Broadband deployment in rural areas is however a costly business. Market forces alone have proven incapable of stimulating broadband rollout at the expected pace set by the Community. The question is what possibilities Member States have when a market failure is discovered.

State aid, granted to projects promoting deployment of broadband infrastructure, is considered an appropriate means to battle market failure if: the measure concerns regions that are commercially unattractive; an open tender procedure, according to the Community rules on public procurement, has been used in choosing a service provider; mechanisms to avoid over-compensation are present; competitors are allowed equal access to the established infrastructure; the project is technologically neutral; granted funds are put into separate accounts and the amount and duration of the funding is limited. The important Community objective of “Broadband for all” can thus be achieved in a manner which does not unduly distort competition.

The Swedish model for granting State aid to broadband deployment seems to be compatible with EC Law. Despite the fact that the model has never been notified to the Commission, it is in line with the criteria established through the Commission’s practice.

Economic theory has been given an increasingly prominent role within EC Law – especially within Competition Law. A strictly legal perspective has given way to economic analysis in this field. The sector of electronic communications, which is characterised by rapid and disruptive change, needs flexible legislation capable of adapting itself to the constantly changing preconditions. Legislation needs to be managed by objectives, and not designed in terms of rigid laws, if Community objectives are to be fulfilled. State aid granted to broadband deployment in rural areas can, in this view, produce a competitive market instead of distorting competition, which has been the Commission’s traditional opinion of State aid.

Sammanfattning

Den här uppsatsen handlar om EG-rättens inställning till statsstöd som ges till bredbandsutbyggnad i glesbygd. Syftet är att undersöka huruvida gemenskapsrätten tillåter att enskilda medlemsstater beviljar statsstöd till bredbandsprojekt, och i så fall under vilka förutsättningar stödet anses vara förenligt med EG-rätten. Fokus ligger på situationen i Sverige, satt i relation till EU15.

Tillgång till bredband är en viktig fråga för den Europeiska Unionen, eftersom bredband har en förmåga att stimulera både ekonomisk tillväxt och social sammanhållning. Bredbandsutbyggnaden är dock dyr i glesbefolkade områden, och marknaden har visat sig vara oförmögen att stimulera utbyggnad i glesbygd i takt med gemenskapens målsättning. Frågan är vad medlemsstaterna kan göra då ett marknadsmisslyckande kan konstateras.

Statsstöd fastslås vara ett lämpligt medel för att komma tillrätta med marknadsmisslyckanden om de: ges till infrastrukturprojekt i kommersiellt oattraktiva regioner; tilldelas genom offentlig upphandling; inte medför överkompensation till den utvalda entreprenören; ger alla operatörer likvärdig tillgång till den etablerade infrastrukturen; ges till projekt som är teknologiskt neutrala; sätter tilldelade medel i avskilda konton hos entreprenören och är begränsade till både storlek och löptid. Det viktiga gemenskapsmålet ”bredband till alla” kan i sådana fall uppnås med hjälp av statsstöd, på ett sätt som inte snedvrider konkurrensen på ett olämpligt sätt.

Sverige har ett regelverk kring statsstöd till bredbandsprojekt som verkar stämma väl överens med EG-rättens regler på området. Trots att den svenska statsstödsmodellen inte formellt meddelats kommissionen, uppfyller den många av de krav som kommissionen utvecklat i sin beslutspraxis.

Inom EG-rätten har ekonomisk teori fått allt större fotfäste, särskilt inom konkurrensrätten. För att uppnå gemenskapens målsättningar krävs numer att hänsyn tas till ekonomiska konsekvenser. Ett strikt juridiskt perspektiv har fått ge vika för en ekonomisk marknadsanalys. Detta är inte minst viktigt inom sektorn för elektroniska kommunikationer, där den tekniska utvecklingen är snabb och omvälvande. Strikta juridiska regelverk och prövningar kan här inte bidra till att gemenskapsmålen uppnås, utan dessa metoder får ge vika för en mer verklighetsbaserad avvägning och bedömning. Statsstöd som ges till bredbandsutbyggnad i glesbygd kan genom detta synsätt bidra till att konkurrensutsätta marknaden, istället för att snedvrida konkurrensen så som kommissionen traditionellt ansett.

Preface

I would like to thank Björn Björk and Ellen Hausel-Heldahl for taking the time to meet me and answer my questions. Having access to two national experts has been extremely inspiring, and with your aid I hope I have been able to put my thesis on a decent level.

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Lisa Gurner Björk

Abbreviations

BT	British Telecom
CDC	Caisse des Dépôts
CFI	Court of First Instance
Commission	Commission of the European Communities
DSL	Digital Subscriber Line
EC	European Community; <i>also</i> Treaty establishing the European Community
ECJ	European Court of Justice
EP	European Parliament
EU	European Union
EU15	The 15 Member States of the EU before the enlargement in 2004
EU27	The 27 Member States of the EU after the last accession in 2007
European Courts	European Court of Justice and Court of First Instance
GNP	Gross National Product
GPT	General Purpose Technology
ICT	Information and Communication Technology
IT	Information Technology
kbps	kilo byte per second
LEK	Lag (SFS 2003:389) om elektroniska kommunikationer, the Swedish Act on Electronic Communications
MAN	Metropolitan Area Network
PSO	Public Service Obligation
PSTN	Public Switched Telephony Network
PTS	Post- och telestyrelsen (National Post and Telecom Agency)
ROI	Return On Investment
SAAP	State Aid Action Plan
SGEI	Service of General Economic Interest
SGI	Service of General Interest
SKL	Sveriges Kommuner och Landsting (The Swedish Association of Local Authorities and Regions, SALAR)
SMP	Significant Market Power
USO	Universal Service Obligation

1 Introduction

“Broadband access [...] has become a prerequisite for everything from economic growth to social inclusion.”¹

1.1 Purpose

Broadband access is a highlighted policy area of the **European Union (EU)** because of its ability to enhance economic growth and social cohesion. Nevertheless, broadband deployment is a costly business. Market forces alone have proven incapable of stimulating broadband rollout at the expected pace set by the Community. In a similar situation, it seems like a good solution to grant State aid to projects concerning broadband deployment. Or does it?

The policy area of State aid law has virtually exploded during the last decade. The Commission has been very active in trying to create a coherent Community policy, but the issue State aid control is full of political and social considerations. One Member State’s subsidy can for example entail another Member State’s unemployment. More importantly, if public funding should be allowed in the EU, it is vital to ensure that the granted aid is compatible with the objectives of the Common Market.

The Internal market is based on the idea that market forces should be the principal forces that regulate the provision of commodities, goods and services in the Member States. The Competition policy of the Community is based on the idea that a market-based economy is the best guarantee for raising living standards in the EU – and raising living standards to the benefit of its citizens is one of the primary objectives of the EU, as expressed in the Treaty.² For this reason, public intervention on the Internal Market poses the question whether projects, funded by public grants, are compatible with the European Community rules on competition in general, and the rules on State aid in particular.

The idea that only market forces should control the market is an ideal theory, which in many situations does not work due to market failure. Broadband deployment in rural areas is one field where the commercial market has proven itself unable to meet the general objectives of society in the European Union. It is difficult to find operators willing to take the risks of financing broadband infrastructure in sparsely populated territories, due to slow or even hazardous **return on investments (ROI)**. Within

¹ The European Commission’s webpage on the Information Society, http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm.

² *European Union Consolidated Versions of the Treaty on European Union and of the Treaty Establishing the European Community*, Official Journal C 321 E/1.

Community Competition law, State aid control has served an important role in promoting broadband, alongside antitrust rules.³

Today, achieving broadband deployment in areas with market failure is one of the three most important pillars of the i2010 policy.⁴ Broadband is regarded as a prerequisite for better quality of life, better environmental standards, prosperity and sustainable growth. Broadband deployment is also vital in making public and social services equally available to all citizens – individuals and companies alike.

An important reason for why broadband rollout is an issue of highest priority in the Community is that broadband, as an **Information and Communication Technology (ICT)**, represents a so called **General Purpose Technology (GPT)**. A GPT does not belong to a particular sector of the economy. On the contrary, many other sectors can benefit from the technology of a GPT. Specially regulated sectors such as underdeveloped regions, the transport sector, research and development, broadcasting and the energy sector are all policy areas that would benefit directly from widespread broadband access.

As late as in 2005, the Commission reported that there was a significant gap between urban and rural areas in the EU15.⁵ Since then, the EU has grown by twelve Member States. In May 2007, the Commission stated that there is an even larger gap between urban and rural areas in the EU27. Since the market has failed to promote broadband deployment in rural areas, public intervention in terms of State aid is necessary to achieve the objectives of the Community's policies – but the question remains *how* this public intervention should be carried out, so that the granted State aid does not distort competition but rather enhances it. This brings us to the question of how to design a system of legal principles to ensure the competitive use of public funding of broadband deployment.

This thesis sets out to discover how the EC rules on State aid to projects regarding the deployment of broadband infrastructure has developed. In particular, three areas will be examined:

- What is the importance of electronic communications for the development of society of today? What is the significance of broadband deployment for the development of electronic communications?
- How and why does the market fail to achieve broadband deployment in rural areas? What kind of imperfections are inherent in the market, and which possible solutions are available? Is the use of State aid

³ http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm.

⁴ For an explanation on i2010, see Chapter 2.3.1.3.

⁵ Communication from The Commission to The Council, The European Parliament, The European Economic and Social Committee and The Committee of the Regions, *Bridging the Broadband gap*, COM(2006) 129 final, p. 5.

beneficial in resolving a market failure of providing society with broadband communications? If so, under which circumstances is State aid appropriate, and how is the market expected to act?

- Which possibilities do Swedish local and regional authorities have to act on this type of market failure? Can they grant aid to the rollout of broadband infrastructure? If so, how should they safeguard compatibility of the granted aid with Community rules?

1.2 Method and Material

This thesis is written with a traditional dogmatic method. Available sources of law will be examined in order to discern the rules that apply to the policy areas in question. These rules will be systematised and analysed.

The materials used are:

- **basic textbooks** on EU law, providing the basic background of EC law and giving references to other publications.
- **specific textbooks** on EC State aid law. Most of the textbooks that have been used are somewhat outdated (see below), but they have been useful in mapping the general background.
- **articles** from national and international publications. Most of the articles used are recent, and thus more updated on the subject than the textbooks mentioned above.
- **secondary legislation** and other **EU documents** from the Commission and other EU institutions, providing the background for the political motives behind the legislation (and lack thereof) on State aid and also showing the evolutionary progress that has taken place in this field of law.
- **interviews** with two Swedish experts on the area of broadband deployment and State aid respectively, in order to better grasp the difficulties inherent in the policy areas.

I have decided not to use material older than 5 years, except when checking references and tracing the background for the present Community position. The reason for this is that the discipline of State aid, in the context of **services of general economic interest (SGEI)** in general and broadband deployment in particular, has evolved rapidly during the past decade due to the parallel swift development of technology and society. Access to broadband is still such a recent phenomenon that older material would not be helpful in analysing the present situation, which is what I am interested in doing.

1.3 Delimitations

I have chosen not to analyse procedural rules concerning State aid in detail, even if Article 86 EC will be discussed in the context of SGEI.

I have decided to focus on the European Union's policies on **broadband deployment** (supply side), and not broadband usage (demand side), since it is the deployment that attracts State aid. For the same reason I have chosen not to examine the particular services offered over the deployed infrastructure.

The thesis concerns broadband deployment in **rural areas**. Urban areas have inherent characteristics that in most cases result in a competitive market situation. Densely populated areas automatically give incitements for one or more operators to be active, which makes market failure less probable. Rural areas, on the other hand, are interesting to focus on because of their likelihood to have low or no competition.

The analysis will focus on broadband deployment **in Sweden**. The situation in Sweden will be related to that of the EU15, since there is not yet sufficient data available on broadband issues for the EU27. Also, the Member States of EU15 have fairly comparable situations regarding their markets for broadband, as opposed to the newer Member States. These countries have had a different pace in introducing broadband strategies, and the infrastructural preconditions (such as the (non-)existence of a metallic access network or **Public Switched Telephony Network, PSTN**) are different. This brings about a different pattern of development, where other technological solutions might be preferred.⁶

1.4 Disposition

The introductory chapter addresses issues of purpose, method and material, delimitations, disposition and various definitions that will help the reader to better understand the language used in the area of State aid law, SGEI and broadband deployment.

Chapter two of the thesis consists of a general background to the area of State aid law, the Community policy on SGEI and its policy on the deployment of broadband infrastructure. These three issues will be described in terms of relevant Treaty Articles, the work of the Commission

⁶ In the new Member States, the broadband market is just starting to develop. Among other things, lower levels of PC and telephone line penetration restrict this development. Furthermore, the new Member States have a clear trend of mobile take-up instead of fixed line telephony. This is a situation in which wireless solutions probably will play a more important role than fixed line in providing broadband services. Existing TV cable networks are an important alternative to the upgrading of telephone networks, whereas the broadband rollout in the EU15 is mostly based on upgrading telephone networks. In the new Member States, the issue is more about a slow adaptation to the market – not a market failure. *Bridging the Broadband gap*, p. 6.

within the particular field and, where available, the case-law of the European Courts. The last part of each section describes the situation in Sweden and how each particular issue has been received there.

The third chapter presents an assessment of the questions posed in the introduction.

Chapter four offer an analysis of the current legislation and of possible solutions to the thesis questions.

The last chapter of the thesis presents the conclusions I have drawn during the course of my work.

1.5 Definitions

This section provides some basic information on State aid law, SGEI and the characteristics and technicalities of broadband.

1.5.1 The Position of State Aid

Strengthening the regional economy is an important objective of the EU. In order to achieve this, measures providing individual undertakings with State aid can be used in order to enhance their competitiveness. This does, however, entail distortion of competition, as businesses not granted State aid are discriminated against, and this could lead to an unwanted malfunctioning of the internal market. So how does the Community deal with the problem?

State aid control was introduced as a key pillar of Competition law in the European Community as early as the Treaty of Rome, signed in 1957 (hereinafter referred to as the Treaty).⁷ The Treaty does not impose a total ban on State aid. Even if State aid is in principle regarded as incompatible with the Common market, it can nevertheless be justified in exceptional circumstances.⁸ The main provisions on State aid are found in the Chapter on Rules on Competition. The main goal of the Chapter is to avoid distortion of competition in the Common Market.

The State aid framework consists of an obligation for the Member States to notify the Commission of planned State aid, and a standstill clause that forbids the implementation of a grant before the Commission has approved of the measure. Within this framework, State aid law has developed through the practice of the Commission and the jurisprudence of the European Courts.⁹

⁷ See note 2.

⁸ Vademecum Community Rules on State Aid, 15/02/2007, available at http://ec.europa.eu/comm/competition/state_aid/studies_reports/vademecum_on_rules_2007_en.pdf, p. 2.

⁹ Biondi, Eeckhout & Flynn, p. 117.

The Treaty gives the Commission the responsibility for State aid control, and the area of State aid law has progressed rapidly during the 21st century. The most important developments have been the launching of the Commission's **State Aid Action Plan (SAAP)**¹⁰ in 2005; a debate on the role of economic analysis in State aid control; a large number of State aid cases in the European Courts and a large number of rulings adopted at national level in the Member States.¹¹

Today, the European Courts and the Commission have adopted a broad view of what is included in the concept of State aid. When assessing whether a measure constitutes State aid or not, focus is on its consequences – not its legal form.¹² One purpose of the State aid rules is to allow the Commission “*to maintain a level playing field between the Member States, no matter their different levels of resources and different traditions of State intervention.*”¹³

The Community rules on State aid are, according to the Commission, important since they play a key role in managing a necessary economic reform within the Union. This reform is needed due to slow growth, lasting budget deficits, high unemployment and aging populations in the Member States.¹⁴

1.5.2 Services of General Economic Interest

The term “services of general economic interest” is used in Articles 16 and 86 EC, but the concept is not clearly defined in the Treaty. Nor is it defined in secondary legislation, but according to Community practice the term refers to services of an economic nature that are subject to specific **public service obligations (PSO)** by virtue of a general interest criterion.¹⁵ Access to SGEI are considered fundamental rights in the EU,¹⁶ and the concept covers in particular certain services provided by the large network industries, such as transport, postal services, energy and communications. The term also extends to any other economic activity subject to PSO. Both the Community and the Member States can define a SGEI, but the Member States have been given a wide discretion in this field. The concept is adaptable and flexible in line with changes in society and the market.¹⁷

¹⁰ COM(2005) 107 final, *State Aid Action Plan, Less and better targeted state aid: a roadmap for state aid reform 2005-2009*.

¹¹ Hancher, Ottervanger & Slot, p. 7.

¹² Craig & de Búrca, p. 1141.

¹³ *State Aid Action Plan*, paragraph 9.

¹⁴ Neelie Kroes, European Commissioner for Competition, Speech/05/440: *The State Aid Action Plan – Delivering Less and Better Targeted Aid*, UK Presidency Seminar on State Aid, London 14th July 2005.

¹⁵ SGEI and PSO are virtually the same thing. See Hancher, Ottervanger & Slot p. 65.

¹⁶ See COM (2001) 598 final, Report to the Laeken European Council, *Services of General Interest* and <http://europa.eu/scadplus/leg/en/lvb/l26087.htm>.

¹⁷ COM(2004) 374 final, *White Paper on services of general interest*, Annex 1.

SGEI should not be confused with the broader concept of **services of general interest (SGI)**. This term is not used in the Treaty, but it is derived from the concept of SGEI. SGI covers both market and non-market services, classified by public authorities as being of general interest and subject to specific public obligations. The economic element of SGEI is not present in the concept of SGI.¹⁸

The concept **universal service** includes a set of basic telecommunication services. These should always be available to citizens of the EU at a determined quality and an affordable price, even when the market fails to provide this. At present, the concept includes voice telephony and a minimum speed connection to the Internet.¹⁹ Broadband access is not included. A **universal service obligation (USO)** is an obligation to perform a universal service.

The term **public-private partnership (PPP)** refers in general to different forms of cooperation between public and private sectors. The concept is not defined at Community level, but PPP's aim at ensuring the funding, construction, renovation, management or maintenance of an infrastructure or the provision of a service.²⁰

1.5.3 What is Broadband?

To be connected to an electronic communication network, in order to get access to the Internet, with the ability to send and receive data, is an **electronic communication service**. **Narrowband** is an older basic service of this kind, consisting of a "dial-up" connection with limited capability of sending and receiving data. **Broadband** is a recent and more advanced, "always-on" Internet connection, allowing high-speed data transmissions of larger volumes with a minimum of delay.²¹

Broadband networks typically consist of a national **backbone**, a regional and a local **backhaul** and an **access network** (or **local loop**) connecting the consumer. Technologies using **optical fibre** allow the highest bandwidth to be used, and these technologies are generally deployed for national and regional networks. The connection to the final user, called the **last mile**, can then be provided over other technologies, for instance through the existing copper telephone lines (the **metallic access network** allows for the **xDSL**

¹⁸ *White Paper on services of general interest*, Annex 1.

¹⁹ http://ec.europa.eu/information_society/policy/ecomm/todays_framework/universail_service/index_en.htm. See also Directive 2002/22/EC on universal service and users' rights relating to electronic communications networks and services (Universal Service Directive).

²⁰ http://ec.europa.eu/internal_market/publicprocurement/ppp_en.htm.

²¹ Hencsey et al, p. 8; COM(2004) 369 final, *Connecting Europe at High Speed: National Broadband Strategies*, p. 3. According to a definition, made by PTS, which is in line European standards, the transmission rate of broadband should be at least 2 Mb per second, PTS-ER-2007:7, *Förslag till bredbandsstrategi för Sverige*.

technology), through TV cable networks, wireless solutions, customised fibre access solutions, satellite or electrical powers.²²

In rural areas, commercial incentives to finance broadband deployment often prove to be insufficient. The deployment of broadband networks is connected with high fixed costs, making it more cost effective to build in densely populated areas with strong demand. 65-70% of the costs associated with broadband deployment are related to civil infrastructure such as establishing ducts and power supplies. In areas of low demand, where the coverage of cost is difficult to ascertain, private operators are unwilling to invest in infrastructural projects with long periods of amortisation.²³

Black areas refer to areas where demand is high, thus supporting a competitive supply. **Grey areas** are areas of lower demand, but still enough to create natural monopolies where a single operator can refuse to let other operators access its basic infrastructure. **White areas** are areas where there is no broadband provision at all.²⁴

Platforms are communications network technologies. These can feature either fixed or radio-based transmission infrastructure, and different platforms can substitute or supplement each other depending on the particular situation. The technological development of platforms is rapid, which means that new solutions are invented and made available continuously. Civil engineering costs can be kept low if existing infrastructure (for example energy, water and/or transport infrastructure) is exploited for the deployment of new platforms.²⁵

There is no specific platform that will offer the best solution in all cases, since the technologies are dependent on the characteristics of each location. The optimum connectivity can however often be achieved through a combination of technologies and solutions. The Commission regards the local authorities to be the best judges of which platform/s would be the optimum for their region. Investment plans and the choice of platform should be made on the basis of current availability and effective demand.²⁶

²² Hencsey et al, p. 8. DSL is the predominant access technology in the EU – 80% of the total broadband lines use this technology. Cable modem is the second most important technology in terms of penetration, with a share of 18%. *Bridging the Broadband gap*, p. 5.

²³ Hencsey et al, p. 9, *Bridging the Broadband gap*, p. 5.

²⁴ Hencsey et al, p. 9.

²⁵ *Bridging the Broadband gap*, p. 6-7.

²⁶ *Ibid*, p. 7.

2 Background

The following subchapters will provide a general background to the areas of State aid law, SGEI and the Community policy on broadband deployment respectively.

2.1 State Aid

This chapter consists of a summary of the most important rules of State aid law.²⁷

2.1.1 The EC Treaty

As already mentioned in Chapter 1.5.1, the two fundamental rules of State aid control are the obligation to notify and the standstill clause.²⁸

In Article 87 EC, the Commission is given a rather wide discretion to assess whether particular State aid is compatible with the Common Market. The principle behind the Article is that any distortion of competition, resulting from granted State aid, should be balanced against the perceived benefit that the aid could give in pursuing important Community objectives.²⁹

State aid may be declared compatible with the Treaty if it fulfils clearly defined objectives of common interest. In addition, it must not distort competition to an extent that is counterproductive for the objectives of the Community.³⁰

State aid rules apply to measures that satisfy four conditions listed in Article 87(1) EC. To assess whether a State aid is incompatible with the Treaty, it needs to be established that:

1. there is a transfer of State resources in any form;
2. the aid granted entails an economic advantage that the recipient would not have achieved otherwise;
3. the aid is selective in any form (for example favouring certain regions, undertakings or the production of certain goods), and
4. the aid potentially affects trade between the Member States.³¹

These elements are interdependent, which means that they have to be examined together in order to establish whether they occur or not.³² A

²⁷ For a more detailed discussion on State aid rules, see for example Hancher, Ottervanger & Slot.

²⁸ These rules can be found in Article 88 EC, but since they are of procedural nature they will not be discussed further.

²⁹ As Neelie Kroes put it in Speech/05/440: *The State Aid Action Plan – Delivering Less and Better Targeted Aid*: “Assessing the compatibility of State aid is fundamentally about balancing the negative effects of aid on competition with its positive effects in terms of the common interest.” See also Biondi, Eeckhout & Flynn, p. 118.

³⁰ *State Aid Action Plan*, paragraph 10.

³¹ *Vademecum Community Rules on State Aid*, pp. 2-4.

measure that fulfils all of the above listed criteria is normally incompatible with EC law and prohibited as such by the Treaty. The criteria have been widely defined, so it is in reality rather easy for a measure to fall under the State aid prohibition.

2.1.2 The Work of the Commission

The Commission is the primary decision-maker in the area of State aid law, and the Treaty gives the Commission the option of developing the policy on State aid through formal legislation or informal rule-making (i.e. individual Decisions).³³ The Commission has chosen to develop State aid law mainly through Guidelines and Decisions. Guidelines are reviewed on a regular basis, making it possible for this kind of soft law to adapt to the rulings of the European Courts as well as to changes in society and the Common Market.³⁴ The Commission's primary motive with the State aid policy is to modernise the rules while maintaining strict control over granted State aid.³⁵

The Commission's soft law aims at clarifying the margin of the Commission's discretion, making it easier for Member States to predict how the Commission will assess the compatibility criteria authorising State aid.³⁶ Assessment criteria for many different kinds of aid can thus be found in the soft law.³⁷

The SAAP³⁸ was created due to an urgent need to streamline the Community's State aid policy. The previous regime was complex, and consisted of many different documents adopted by the Commission. One objective of the SAAP was to focus the attention on the most distortive types of State aid. Another was to make the State aid rules more predictable and user-friendly, with improvements of legal predictability and a decrease of the administrative burden.³⁹ The SAAP is a comprehensive reform of the State aid policy, and a direct contribution to the renewed **Lisbon Agenda**.⁴⁰

³² Biondi, Eckhout & Flynn p. 5.

³³ Craig & de Búrca, pp. 1138-1139.

³⁴ Biondi, Eckhout & Flynn, p. 119. Guidelines, frameworks, notices or communications are all known as soft law, but they have no internal hierarchy – the various forms of soft law have equal status. Within State aid law, guidelines and frameworks have been utilised for focusing on compatibility criteria for traditional types of aid, and notices have been used when the texts focus on certain types of aid (for example fiscal aid, guarantees). See Biondi, Eckhout & Flynn p. 118.

³⁵ Ibid, p. 118.

³⁶ Ibid, p. 122.

³⁷ Ibid, p. 118.

³⁸ See note 10.

³⁹ *State Aid Action Plan*, paragraph 17. Neelie Kroes has further explained that the previous framework was an unnecessarily complicated set of rules, exemptions and guidelines, with cumbersome and lengthy procedures. The system was perceived as bureaucratic, and it was as difficult to get approval of small as well as large sums of State aid (despite the fact that the latter ones are potentially more distortive). Speech/05/440: *The State Aid Action Plan – Delivering Less and Better Targeted Aid*.

⁴⁰ The Lisbon Agenda sets out the EU's policy priorities for the next decade. The main objectives are to make Europe the most competitive and dynamic knowledge-based economy in the world, with a growth in jobs and increased social cohesion as important

The new regime aim at giving the Member States the possibility to use scarce state resources where they can have the most impact.⁴¹ The system is designed to be transparent, user-friendly and proportionate, with extra care taken to the adherence to the principle of subsidiarity. Member States are encouraged to cooperate with each other and with the Commission.

In short, the reform package presented in the SAAP is based on:

- less and better targeted State aid;
- a refined economic approach;
- more effective procedures, better enforcement, higher predictability and enhanced transparency; and
- a shared responsibility of the Commission and the Member States, which means that the Member States have to support the developed State aid regime and commit to comply with the rules.⁴²

In order to be able to disregard certain aid measures, the Commission has established a number of exemptions from the general prohibition on State aid. For example, small amounts of aid (called **de minimis** aid) are exempted from the scope of Article 87(1) EC. Article 87(2) and (3) EC provides further exemptions from the strict prohibition of incompatible aid. These exemptions will not be discussed in detail, but some of them are important to note in the context of broadband deployment. For example, **regional aid** given to areas that are underserved according to EU or national standards is allowed, and **block exemptions** have been issued as regards aid to the provision of SGEI.⁴³

effects. See Lisbon European Council 23 and 24 March 2000, Presidency Conclusions at http://www.europarl.europa.eu/summits/lis1_en.htm and European Council 23 and 24 March 2006, Presidency Conclusions "Re-launched Lisbon Strategy for Jobs and Growth", available at http://www.europarl.europa.eu/summits/pdf/bru032006_en.pdf.

⁴¹ Neelie Kroes expresses this as getting the "best value for money for [the] taxpayers". Speech/05/440: *The State Aid Action Plan – Delivering Less and Better Targeted Aid*.

⁴² *State Aid Action Plan*, paragraph 18. The SAAP has been implemented through 2005/842/EC, Commission Decision of 28 November 2005 on the application of Article 86(2) of the EC Treaty to State aid in the form of public service compensation granted to certain undertakings entrusted with the operation of services of general economic interest, based on Article 86(3) EC, which specifies the conditions under which compensation is compatible with State aid rules. A clearly defined public service mandate is needed, and no over-compensation is allowed. Compatible compensation does not have to be notified to the Commission. The SAAP has further been implemented through 2005/C 297/04, the Community Framework for State aid in the form of public service compensation. This framework specifies conditions under which compensation that is not covered by the Decision is compatible with State aid rules. This kind of aid has to be notified since there is a higher risk of distortion of competition. Over-compensation is incompatible with the State aid rules, and it has to be repaid. See Commission press release IP/05/937 "State aid: Commission provides greater legal certainty for financing services of general economic interest". Other measures to implement the SAAP include the Transparency Directive, Commission Directive 2006/111/EC of 16 November 2006 on transparency of financial relations between Member States and public undertakings as well as on financial transparency within certain undertakings. See also Chapter 2.2.2.

⁴³ *Vademecum Community Rules on State Aid*, pp. 4-7. For a further discussion on these types of aid, see Hancher, Ottervanger & Slot.

2.1.3 Relevant Case-Law of the European Courts

The European Courts can judicially review the decisions of the Commission, and have played an important role in clarifying the limits of EC State aid control.⁴⁴

The main cases concerning State aid are *Preussen-Elektra*,⁴⁵ *Ferring*,⁴⁶ *Stardust Marine*,⁴⁷ *Altmark*⁴⁸ and *Pearle*.⁴⁹ These cases concern State aid in various situations, and even if none of them relate to deployment of broadband infrastructure in particular they express basic principles that need to be adhered to in all situations.⁵⁰ The most important case of the above mentioned is *Altmark*, which will be discussed in more detail in Chapter 2.2.3.

2.1.4 The Situation in Sweden

EC State aid law has only been subject to national legislation in Sweden to a limited extent.⁵¹

Kommunallagen, the Swedish Local Governments Act,⁵² is considered to go further than Article 87 EC, providing harsher conditions for local and regional governments to grant State aid to an individual undertaking. In addition, Regeringsrätten (the Swedish Administrative Supreme Court) has given local authorities a very limited scope for granting aid.⁵³ The stricter Swedish rules do not go against EC law, which allows Member States to enforce stricter rules than the ones set out in the Treaty in this area.

Sweden does not have an independent State aid authority. Responsibility for notification and communication with the Commission has been centralised to one of the government Ministries (currently the Ministry of Enterprise, Energy and Communications). Competence to grant State aid has to some degree been delegated to authorities and county administrations.⁵⁴

⁴⁴ Biondi, Eeckhout & Flynn, p. 117.

⁴⁵ *PreussenElektra AG v Schleswag AG*. Case C-379/98, [2001] E.C.R. I-2099.

⁴⁶ *Ferring SA v Agence centrale des organismes de sécurité sociale (ACOSS)*. Case C-53/00, [2001] E.C.R. I-9067.

⁴⁷ *France v Commission*. Case C-482/99, [2002] E.C.R. I-4397, generally known as *Stardust Marine*.

⁴⁸ *Altmark Trans GmbH and Regierungspräsidium Magdeburg v Nahverkehrsgesellschaft Altmark GmbH, and Oberbundesanwalt beim Bundesverwaltungsgericht*, Case C-280/00, [2003] E.C.R. I-7747.

⁴⁹ *Pearle BV, Hans Prijs Optiek Franchise BV and Rinck Opticiëns BV v Hoofdbedrijfschap Ambachten*. Case C-345/02, [2004] E.C.R. I-7139.

⁵⁰ For further discussions on the mentioned cases, see for example Hancher, Ottervanger & Slot.

⁵¹ Simonsson, p. 622.

⁵² Kommunallag (1991:900).

⁵³ Simonsson, pp. 623-624. See also Simonsson & Öberg.

⁵⁴ Simonsson, p. 638.

Local, regional and government authorities must inform the responsible Ministry of all planned aid measures that might be subject to revision by the Commission. Even so, there are no sanctions or consequences for an authority that does not fulfil this obligation. In cases where Sweden has been criticised by the Commission, this notification to the government has not been made.⁵⁵

2.2 Services of General Economic Interest

This chapter describes the position of SGEI within the EU.

2.2.1 The EC Treaty

In Article 16 EC, the importance of SGEI for the Community is outlined. SGEI are described as promoters of common values as well as social and territorial cohesion. The Article provides a shared responsibility for the Community and the Member States for the operation of SGEI. Within their respective powers, the Community and the Member States shall ensure that their policies enable operators of SGEI to fulfil their missions.⁵⁶

Article 86 EC is the main Article concerning SGEI. In particular, Article 86(2) EC states that undertakings that provide SGEI are subject to the rules on Competition *as long as* these rules do not obstruct the performance of the SGEI. The rules of Competition are flexible however, and Member States can value different objectives according to national or sectoral needs. Three important Competition law principles, which are important in the context of SGEI, are neutrality in relation to whether the undertaking concerned is private or public (Article 295 EC), the Member States' discretion to define what they regard as SGEI, and that the potential distortion of competition must be proportional in relation to the importance of the SGEI performed.⁵⁷

2.2.2 The Work of the Commission

The Commission has been very active in trying to clarify the rules regarding SGEI. A long list of documents has been produced for this reason, among which the SAAP is the most important.⁵⁸ In the SAAP, the Commission states that the *“provision of effective and high quality [SGEI] is a key component of the European welfare state and is essential for ensuring social and territorial cohesion [...] and for the exercise of an effective citizenship. High quality SGEI also contribute to the competitiveness of the European economy.”*⁵⁹

⁵⁵ Simonsson, p. 627.

⁵⁶ *White Paper on services of general interest*, p. 5-6.

⁵⁷ See <http://europa.eu/scadplus/leg/en/lvb/l26087.htm>.

⁵⁸ See, among others, *White Paper on services of general interest*.

⁵⁹ *State Aid Action Plan*, paragraph 33.

The implementation of the SAAP has, among other things, resulted in the **SGEI Decision**, the **Framework** for State aid in the form of public service compensation and the **Transparency Directive**⁶⁰.

The Decision clarifies when compensation for the provision of SGEI is compatible with the State aid rules, and thus does not have to be notified to the Commission. The Decision highlights the *Altmark*-criteria of a clearly defined public service mandate and no over-compensation (see Chapter 2.2.3).

The Framework clarifies when compensation not covered by the Decision is compatible with State aid rules, but nevertheless needs to be notified to the Commission due to a high risk of distortion of competition. Again, no over-compensation is emphasised along with the principle of no cross-subsidising, which means that an undertaking should not be allowed to use State aid on other markets than the one specified in the measure.

The Transparency Directive stresses that undertakings, which perform PSO at the same time as conducting normal market transactions, should keep separate accounts for their received public funds. Again, this is a safeguard against over-compensation.

2.2.3 Relevant Case-Law of the European Courts

The CFI has established that compensation given to an undertaking for the provision of PSO is State aid according to Article 87(1) EC.⁶¹ As described in Chapter 2.1.1, all aid measures that fulfil the conditions in Article 87(1) EC are subject to the rules on Competition, but SGEI rarely fulfil the criteria of economic advantage and effect on Community trade. Compensation may thus be compatible with the Common market if it fulfils the conditions of either Article 86 EC (that the rules on Competition are applicable insofar as they do not hinder the performance of assigned PSO) or Articles 87(2) and (3) EC (the State aid measure is of social character or aims at aiding the development of certain businesses/regions etc – for a full list, see Article 87 EC). Compensation needs to be notified to and approved by the Commission in order for it to be considered a compatible aid measure. The exemptions described in Chapter 2.1.1 are vital.⁶²

The landmark ECJ judgment of *Altmark*⁶³ introduced four cumulative criteria that have to be fulfilled in order for a measure to be considered as compensation for discharging a PSO (and thus not State aid that needs to be notified). The following conditions must then be fulfilled:

⁶⁰ See note 42.

⁶¹ Case T-106/95, *FFSA and others v Commission*, [1997] E.C.R. II-00229.

⁶² See <http://europa.eu/scadplus/leg/en/lvb/l26087.htm>.

⁶³ See note 48.

1. the recipient undertaking must be required to perform PSO that have been clearly defined;⁶⁴
2. the parameters on basis of which the compensation is calculated must be established beforehand in a transparent and objective manner;
3. the actual compensation given cannot exceed what is necessary to cover the costs incurred (taken into consideration the relevant receipts and a reasonable profit); and
4. if public procurement was not used for assigning the PSO to an undertaking, the level of compensation needed must have been determined on the basis of an analysis of the costs which a typical undertaking would have incurred in discharging those PSO.

2.2.4 The Situation in Sweden

Article 86 EC has no equivalent rule in Swedish law. The meaning of the Article has not been implemented in the Swedish legislation, and there are no national laws on the subject. There is a low awareness of Article 86(2) EC in the Swedish legal community, and it has been argued that this creates a risk that the Article is overlooked by appellants, defendants and courts alike in national proceedings.⁶⁵

2.3 Policy on the Deployment of Broadband Infrastructure

This chapter presents the EU policy on the deployment of broadband infrastructure. There are no specific rules on broadband in the Treaty, which is why the focus of the chapter lies on the work of the Commission.

2.3.1 The Work of the Commission

Quoting its own webpage on the subject, “[t]he Commission has decided to combine all EU policy instruments that have an impact on broadband development in order to promote and encourage broadband penetration in the EU.”⁶⁶ The Commission has addressed the importance of broadband rollout in a number of Communications and Decisions.⁶⁷

⁶⁴ This can be seen as an implicit requirement that the service in question is a SGEE. Hencsey et al, p. 10.

⁶⁵ Simonsson, p. 637.

⁶⁶ http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm.

⁶⁷ For further information, apart from what will be discussed in this Chapter, see COM(2003) 65 final, *Electronic Communications: the Road to the knowledge Economy*; COM(2003) 673 final, *White Paper Space: a new European frontier for an expanding Union. An action plan for implementing the European Space Policy*; COM(2004) 61 final, *Connecting Europe at high speed: recent developments in the sector of electronic communications*; *Connecting Europe at High Speed: National Broadband Strategies*; COM(2004) 380 final, *eEurope 2005 Action Plan: An Update and Bridging the Broadband Gap* p. 7.

2.3.1.1 The Concept of the Information Society and the Need for Broadband

From the Commission's point of view, broadband is the key to achieving the objectives of the Lisbon Agenda – in particular the development of the **Information Society** and of the **e-economy**.⁶⁸ The realisation of both these visions is dependent on the existence of adequate infrastructure for electronic communications. As mentioned above, broadband is considered to be the best deployable technology, so the existence of broadband infrastructure is crucial for the development of the Information Society and the e-economy.

In addition, rural areas are considered to benefit more from broadband deployment than urban areas, since broadband can provide the vital link to the rest of society for these areas. This link is an essential factor in attracting businesses as well as providing government services of all kinds.⁶⁹

In sum, broadband is seen as an enabling technology that fuels productivity and growth as well as entailing developments that benefit businesses, administrations and consumers. Broadband services are considered to create new markets, increase the productivity of workers and add value to business performance and public efficiency as well as increase quality of life. To control, encourage and improve broadband deployment is therefore crucial.⁷⁰

2.3.1.2 State Aid to Infrastructure Projects in General

If three particular conditions are fulfilled, the funding of an infrastructure project falls outside the definition of State aid, and thus does not have to be notified to the Commission. These conditions are that:

1. the project must concern the provision of an SGEI or a responsibility of the State vis-à-vis the public;
2. the market fails to provide the same infrastructure under the same conditions; and
3. the infrastructure must be available to competitors, i.e. it must not be discriminatory.⁷¹

Public funding of infrastructure such as roads and bridges is normally not considered State aid.⁷²

⁶⁸ For more information on these issues, see the Commission's Thematic Portal on Europe's Information Society at http://ec.europa.eu/information_society/index_en.htm; COM(2001) 711 final, *The impact of the e-economy on European Enterprises: economic analysis and policy implications* and <http://ec.europa.eu/enterprise/ict/policy/e-economy.htm>.

⁶⁹ *Bridging the Broadband gap*, p. 4. Furthermore, "[o]ne primary motive for supporting broadband deployment is that broadband connections can help especially rural areas to attract new businesses, upgrade existing businesses, facilitate people's access to authorities, education and health care and enable tele-working."

http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm.

⁷⁰ *Connecting Europe at High Speed: National Broadband Strategies*, pp. 3 and 21-22.

⁷¹ Koenig & Kiefer, p. 416.

⁷² See Anestis, Mavroghenis & Psaraki.

2.3.1.3 State Aid to the Deployment of Broadband in Particular

Through its policy documents, the Commission's view on State aid to the rollout of broadband can be discerned. In **eEurope 2005**⁷³, the scope for public intervention in rural (or “under-served”) areas is emphasised. The Commission suggests that Structural Funds be made use of in order to bring broadband to disadvantaged areas in the Union. Further clarifications on the availability and compatibility of public funding of broadband projects with the State aid regime can be found in **Guidelines on criteria and modalities of use of Structural Funds for electronic communications**.⁷⁴

i2010 – a European Information Society for Growth and Jobs is an initiative which deals in particular with the issues of both geographical coverage of broadband and the social and economic digital divide.⁷⁵ In order to achieve the goals of i2010, the Commission has urged the Member States to adopt and implement **national broadband strategies**.⁷⁶ These strategies aim at accelerating the deployment of broadband infrastructure through stimulating the market in terms of both supply and demand.⁷⁷ The national strategies shall establish goals regarding the broadband coverage. These goals should be reached through an active partnership with local and regional authorities, for example through PPPs. The Commission encourages the use of national funding, Structural Funds and the Rural Development Fund in order to reach the established goals.⁷⁸ **The European Regional Policy** also actively promotes further broadband deployment to bridge the digital divide between rich and poor regions, urban and rural areas and even within regions.⁷⁹ The national broadband strategies that have been implemented so far recognise that governments have an important task in making sure that broadband coverage is achieved in the presence of market failure. State aid granted with this motive is generally allowed. The implemented strategies recognise that competition is an important factor in encouraging private investment.⁸⁰

⁷³ COM(2002) 263 final, *eEurope 2005 Action Plan*.

⁷⁴ *Guidelines on criteria and modalities of use of Structural Funds for electronic communications*, available at

http://europa.eu.int/comm/regional_policy/sources/docoffic/working/sf2000_en.htm.

⁷⁵ http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm. The broadband availability objective “Broadband for all by 2010” is expressed in i2010. This is the European IT policy. For more information on i2010, see http://ec.europa.eu/information_society/eeurope/i2010/index_en.htm.

⁷⁶ See *Connecting Europe at High Speed: National Broadband Strategies*. In 2003, all EU15 Member States had implemented national broadband strategies.

http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm.

⁷⁷ http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm.

⁷⁸ The strategies should also concern broadband take-up and set clear targets for the connectivity of schools, public administrations and health centres. *Bridging the Broadband gap*, p. 10.

⁷⁹ http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm.

⁸⁰ Furthermore, “[c]urrent initiatives address both the supply and the demand side of the market to stimulate a virtuous circle, whereby development of better content and services depends on infrastructure deployment and vice-versa. Some of [the national] strategies

In its Communication on Bridging the Broadband Gap, the Commission lists State aid and public funding among the instruments that can advance broadband deployment. All levels of government in the European Union are encouraged to be more active in making use of these instruments. In addition, the Commission is concerned about maintaining the dynamic between public and private funding of broadband access. Crowding out effects, where private initiative is pushed to the side by State measures, must be avoided.⁸¹

In an article regarding public funding of broadband services, Anestis et al conclude that the Commission nowadays explicitly recognises the role that State aid has to play in achieving broadband access in rural areas. Competition, in combination with the free market, are the preferred methods for achieving broadband access, but State aid can be used to allow rural areas not to lag behind more developed regions.⁸² When deciding whether the public funding of an infrastructure project is to be considered State aid, a multi-step analysis has to be made. Firstly, an aid measure is normally not regarded as State aid if the prospected infrastructure is open to all undertakings without discrimination. Secondly, even if the planned infrastructure is not open to all, a measure may avoid being State aid if it concerns an SGEI. Here, the *Altmark* test described above must be conducted. Thirdly, a measure may avoid amounting to State aid if it represents a market economy investment, i.e. if the public authorities behave in the same way as a private investor would have done under similar circumstances.⁸³ This criterion is difficult to fulfil when it comes to broadband projects that are completely financed through public funds, but it might happen when PPP's are involved.

If neither of the above situations is at hand, a measure may nevertheless be susceptible to approval by the Commission, but in this case the Commission must be notified of the measure. The Commission is inclined to regard public funding of the deployment of broadband infrastructure as compatible with the State aid rules, as broadband penetration is a highly valued objective of the EU. What the Commission needs to establish is that the market fails to provide broadband connectivity to affordable prices, that the funding is proportionate to the objective (greater broadband access) and that the measure does not distort competition in an unduly way.⁸⁴

The Commission has also, in a number of Decisions, addressed the public funding of broadband projects in the Member States. A State aid policy for publicly funded broadband projects has emerged. In short, State aid has been deemed compatible with the Common Market, or not regarded as State

have been recently revised to introduce more refined targets." *Bridging the Broadband gap*, p. 7.

⁸¹ See Commission press release IP/06/340 of 21 March 2006 "Broadband for all: Commission mobilizes all its policy instruments to bridge the broadband gap". See also Anestis, Mavroghenis & Psaraki.

⁸² Ibid.

⁸³ This is called the "market investor test" and will not be further discussed.

⁸⁴ See Anestis, Mavroghenis & Psaraki.

aid at all (and thus ok for the Member State to put into effect) in rural and remote areas.⁸⁵

In two cases concerning public co-funding of open broadband infrastructures in rural regions of France, the measures constituted compensation for the provision of an SGEI and were thus not regarded as State aid because the *Altmark* criteria were fulfilled.⁸⁶ The only occasion when the Commission concluded that the public funding of a broadband project was incompatible, was in relation to a project in the Netherlands. One of the main reasons for the prohibition is that the Netherlands has one of the most advanced broadband markets in the EU, so the project did not by far address a market failure or concern a less-developed region.⁸⁷

When the Commission assesses whether a measure is State aid or not, and whether the measure is compatible with the Treaty or not, they use a balancing test which consists of three steps. First, the existence of a market failure in relation to a well-defined objective of common interest must be established. Second, it has to be established whether the measure is well-designed in terms of whether State aid is the appropriate instrument, whether it creates an incentive effect and whether it is proportional to its objective (i.e. is the aid kept to a minimum?). Third, it has to be established whether the distortions of competition and effect on trade are sufficiently limited, so that the aid measure is on balance positive.⁸⁸

The Commission has through its Decisions identified a number of indicators that point towards a measure being compatible with the State aid rules. These indicators are that:

⁸⁵ http://ec.europa.eu/information_society/industry/comms/broadband/index_en.htm. See Commission press releases IP/05/530 of 3 May 2005 "State aid: Commission endorses public funding for broadband network in Limousin, France"; IP/04/1371 of 16 November 2004 "Commission approves public funding of broadband projects in Pyrénées-Atlantiques, Scotland and East Midlands"; IP/05/646 of 1 June 2005 "State aid: Commission endorses public funding to bridge broadband communications gap in Wales"; IP/05/1231 of 6 October 2005 "State aid: Commission endorses public funding for broadband communications in Midlands and South West of England"; IP/05/398 of 7 April 2005 "State aid: Commission endorses public funding for broadband communications in rural and remote areas of Spain"; IP/06/284 of 9 March 2006 "State aid: Commission endorses public funding to bridge broadband communications gap in Ireland"; IP/06/755 of 8 June 2006 "State aid: Commission endorses public funding to bridge broadband communications gap in Latvia"; IP/06/949 of 7 July 2006 "State aid: Commission endorses public funding to bridge broadband communications gap in Greece"; IP/05/1331 of 24 October 2005 "State aid: Commission opens inquiry into funding for broadband in Appingedam (Netherlands)" and IP/06/1013 of 19 July 2006 "State aid: Commission prohibits public funding for additional broadband network in Appingedam (Netherlands)".

⁸⁶ Anestis, Mavroghenis & Psaraki.

⁸⁷ Ibid, see also Commission press releases IP/05/1331 of 24 October 2005 "State aid: Commission opens inquiry into funding for broadband in Appingedam (Netherlands)" and IP/06/1013 of 19 July 2006 "State aid: Commission prohibits public funding for additional broadband network in Appingedam (Netherlands)".

⁸⁸ Speech notes, Loretta Dormal Marino, Director DG Competition, *College of Europe Global Competition Law center 3rd Annual Conference Brussels 21-22 September 2006*, available at <http://www.coleurop.be/file/content/gclc/documents/Loretta%20Dormal-Marino.ppt>.

- the funding should concern regions that are underserved in some respect (due to geography, topography, demography, technology etc.),
- the measure should concern regions that are commercially unattractive,
- an open tender procedure according to Community rules on public procurement should be used when awarding the funds to a service provider, as this procedure is likely to minimise the funding granted,
- mechanisms to avoid over-compensation should be present,
- the service provider should allow other operators access to the constructed infrastructure in a transparent and non-discriminatory way,
- the project should be technologically neutral,
- there should be accounting transparency for the granted funds (which is achieved by separate accounts), and
- the amount and duration of the funding should be limited.⁸⁹

2.3.2 Relevant Case-Law of the European Courts

The work of the Commission has not yet been tested in the European Courts. There are no judgments concerning State aid granted to the deployment of broadband infrastructure.

The cases mentioned in 2.1.3 and 2.2.3 do not deal with broadband issues specifically, but the general principles developed through them are applicable to measures granting State aid to broadband projects.

2.3.3 The Situation in Sweden

Even if Sweden is a well-developed country when it comes to broadband accessibility, there are still a number of regions in Sweden that lack access to broadband infrastructure in 2007. In other regions, customers are confined to the services of one single provider. There are about 136,000 households and businesses that lack access to broadband infrastructure altogether.⁹⁰

A policy regime for State aid to broadband deployment was launched by the Swedish government in 2001. The regime focuses on rural areas.⁹¹ It is based on the notion that commercial initiatives should primarily take care of the broadband rollout, but if they fail, public funds can be utilised.⁹² In

⁸⁹ See Anestis, Mavroghenis & Psaraki.

⁹⁰ *Förslag till bredbandsstrategi för Sverige*, p. 3.

⁹¹ In this context, “rural” means less than 3000 inhabitants. Länsenkät per 2006-12-31, *Bredbandsutbyggnad med statligt stöd December 2006*, p. 4.

⁹² *Ibid*, p. 3.

order to achieve the objectives of the policy, a number of laws and ordinances have been created.⁹³

The current regime allows local authorities to initiate, plan and establish deployment of broadband infrastructure in rural areas. In short, local authorities are guided by the following principles. They should identify areas where the market will not supply ICT-infrastructure, and set up IT-infrastructure programmes. They should stimulate competition and avoid distortion of the market by using public procurement (or an open tender procedure) to assign projects (and their funds) to operators, and they should demand that the networks established with the aid of public funds should be open and non-discriminatory towards other operators. The deployed infrastructure must be able to carry an acceptable transmission capacity.⁹⁴

The governmental regional self-administrative agencies Länsstyrelserna (The Swedish County Administrative Boards) are given the task of monitoring the activities of the local authorities. IT-infrastructure programmes established by the local authorities must get the approval of Länsstyrelserna. They also consider applications for public funds, and are able to grant funds if the planned projects meet the legislative requirements. Moreover, Länsstyrelserna control that the local authorities follow the laws and ordinances in this field.

Together with Sveriges Kommuner och Landsting (SKL, The Swedish Association of Local Authorities and Regions) and PTS, Länsstyrelserna monitor and evaluate the public funding of broadband deployment. These organisations cooperate in assessing the level of broadband access every six months, and publish reports on the issue. The Swedish Government uses the reports when discussing budget issues concerning State aid.

⁹³ Lag (2000:1380) om skattereduktion för utgifter för vissa anslutningar för tele- och datakommunikation, Förordning (2000:1469) om stöd till kommuner för anläggande av lokala telenät, Förordning (2001:349) om stöd till kommuner för upprättande av IT-infrastrukturprogram, Förordning (2001:350) om stöd till kommuner för anläggande av ortssammanbindande telenät m.m., Förordning (2003:62) om stöd till kommuner för anläggande av anslutning till rikstäckande telenät, Förordning (2004:619) om stöd till kommuner för etablering av telenät m.m. på orter och i områden där telenätet är eftersatt, Ordinances for extending previous ordinances (2004:991-994) and (2006:1460-1464). In 2003, Lag (2003:389) om elektronisk kommunikation (LEK, The Swedish Act on Electronic Communications) was introduced for the sector of ICT.

⁹⁴ *Bredbandsutbyggnad med statligt stöd December 2006*, pp. 3-4. The Swedish strategy for achieving the "Broadband for all" objective is to increase the accessibility to an infrastructure that can be upgraded to allow transmission rates at a minimum of 2 Mb per second, upstream and downstream, for all permanent households, businesses and public authorities by 2010. *Förslag till bredbandsstrategi för Sverige*, p. 3.

3 Assessment

This chapter will deal with the questions posed in the beginning of the thesis. Different solutions to the problems will be discussed and analysed in the next chapter.

3.1 Electronic Communications as a Fundamental Component of the Information Society

The development of the Information Society, with electronic communications as one of its fundamental pillars, has been rapid over the past few decades. Regardless of transmission capacity, Internet access is today a basic need among the citizens of the EU, and broadband has so far proven to be the best technological solution of electronic communications. Because it offers a high speed, “always-on” connection, broadband is comparably the most secure technology to date.

The EU has, through the Commission, defined and highlighted the capacities and benefits of broadband as a means of electronic communications on several occasions. Its ability to enhance society and spur development towards economic growth makes it one of the main tools in achieving the Community’s objectives. One important economic reason for why broadband is so important for society is its ability to enhance growth. The availability of broadband access can stimulate the establishment of more businesses in a region, which in turn leads to more job opportunities. That will give an incentive for people to move to the region, which will result in an increasing amount of local tax revenues. Local and regional authorities can thereby directly benefit economically from the rollout of broadband.⁹⁵

In sum, broadband is politically considered to be the best solution to the basic public need of access to electronic communications.

3.2 The Use of State Aid in Case of Market Failure

As described in 2.3.1.3, the Commission uses a balancing test when assessing State aid measures. For this reason, it will first be examined how the market for broadband deployment functions in Sweden, and whether this leads to the conclusion that there is a market failure in relation to an

⁹⁵ Interview with Björn Björk, national expert on Information Technology Strategies at the Swedish Association of Local Authorities and Regions, 17 March 2007. This depends, of course, on how taxes are collected. In Sweden, both local and regional authorities have the power to levy taxes besides the national government.

important Community objective. The next step of the balancing test is to ascertain whether State aid is the appropriate instrument in tackling the supposed market failure. Lastly, it will be examined whether the potential distortion of competition is sufficiently limited.

3.2.1 Existence of Market Failure in Relation to a Well-Defined Objective of Common Interest

The previous chapters have clearly shown that broadband access is a well-defined objective of Common interest in the EU. What needs to be established in this step of the balancing test is rather the quest to identify the existence and scope of market failure.

The Commission has defined market failure as “*a situation in which economic efficiency is not achieved owing to imperfections in the market mechanisms*”. This is the case when goods or services are not provided despite existing demand, or when there is a miscalculation of resources and the situation could be improved so that some consumers would be better off, and none would be worse off. The misallocation of resources has to be serious in order to result in a market failure.⁹⁶

As depicted in the previous chapters, broadband infrastructure is not available everywhere in Sweden. The inherent economics of broadband deployment, in combination with Sweden’s geography and demography, has resulted in many grey and black areas where the market is reluctant to provide open broadband infrastructure. According to a mapping made by SKL, there are only commercial incentives for broadband rollout in 20% of Sweden’s geographical surface (which includes some 70% of the population).⁹⁷ In their proposal for a Swedish broadband strategy, PTS notes that the further establishment of broadband networks is seriously hindered or at least slowed down by market barriers. In some areas, private operators have managed to deploy fibre, but this infrastructure is generally owned by the individual constructor and not available to other service providers. In addition, one company dominates the telecom market. TeliaSonera, formerly a State monopoly called Televerket, was for a long time the single operator on the telephony market. When other operators were given the opportunity to enter the market, TeliaSonera was able to maintain a dominant position by owning the infrastructure that had previously been financed by public funds – the metallic access network. This infrastructure carries both telephony and Internet/broadband services. PTS has discovered that TeliaSonera displays discriminatory behaviour.⁹⁸ TeliaSonera’s dominant position on the telecom market is an important reason why the development of open broadband infrastructure is being held back.

⁹⁶ This definition has been made in the context of the risk capital market, but an analogy is appropriate. See Hancher, Ottervanger & Slot p. 111.

⁹⁷ Interview with Björn Björk, 17 March 2007.

⁹⁸ *Förslag till bredbandsstrategi för Sverige*, pp. 4-5.

The provisions of the risk capital market are another reason why private investors are reluctant to finance broadband deployment. Risk capital is generally needed where normal market conditions cause small, innovative and risky businesses to face tremendous problems in attracting investment. The operators of such businesses need to loan money in order to be able to start their projects. The risk capital market is characterised by strong and short termed demands for revenues, and this scheme dictates which projects are considered to be profitable and non-profitable respectively. Long-term projects, which will not be reimbursed until after more than five to seven years,⁹⁹ are considered non-profitable. Ducts, fibre etc. spur high costs that cannot be reimbursed within this time limit. Consequently, loans will not be granted for infrastructural projects that have longer time periods for reimbursement – usually 25-30 years – and the capital owners have, in practice, set a high establishment barrier on the market for broadband deployment.¹⁰⁰

During the past five years, 71% of the investments used for rollout in rural areas of Sweden originate from public funds in various forms – even after open tender procedures.¹⁰¹ The market will consequently finance less than one third of the costs, despite the fact that public procurement has been used in order to ensure a transparent, competitive market situation. This proves that the market will not add funds to broadband rollout in rural areas *even when* the sector is subject to competition and non-distortion of competition is ensured.¹⁰² According to PTS, the availability of broadband infrastructure which allows high transmission rates in all parts of Sweden is a need that cannot be satisfied by market forces alone.¹⁰³

3.2.2 Is State Aid the Appropriate Instrument?

“State aid should only be used when it is an appropriate instrument for meeting a well defined objective, when it creates the right incentives, is proportionate and when it distorts competition to the least possible extent.”¹⁰⁴

Discussing the situation on the Swedish market, a comparison with the Commission’s Decision in *MAN* may be helpful.¹⁰⁵ In this case, Ireland

⁹⁹ According to TeliaSonera’s practice.

¹⁰⁰ Interview with Björn Björk, 17 March 2007.

¹⁰¹ Local authorities contribute with 10%, 53% consist of State aid, 1% comes from State Regional funds and 7% come from the Community Structural funds. This may be compared with the expected figures of 5%, 40%, 7% and 3% respectively. *Bredbandsutbyggnad med statligt stöd December 2006*, pp. 35 and 37.

¹⁰² Operators generally want exclusive rights to the infrastructure they build, in order to ensure profitability. If they do invest in broadband infrastructure on a market where State aid is not involved, the result will be an establishment of parallel networks, which is unprofitable from a national economic perspective, or a grey area with only one active operator. Interview with Björn Björk, 17 March 2007.

¹⁰³ *Förslag till bredbandsstrategi för Sverige*.

¹⁰⁴ *State Aid Action Plan*, paragraph 11.

¹⁰⁵ C(2006)436 final, *Regional Broadband Programme: Metropolitan Area Networks (“MANs”), phases II and III*.

wanted to grant State aid to a project that would install Metropolitan Area Networks (MANs) in regions where there was a market failure of broadband deployment. The former State monopoly, or Incumbent,¹⁰⁶ Eircom was the only operator with infrastructure that would be able to compete with the MANs in the future. There was no infrastructure competition on the market at issue. Eircom offered both retail and wholesale services, but it did not give other operators access to its core infrastructure – its dark fibre. Ireland had no regulations concerning access to Eircom’s infrastructure for other providers, so without the proposed MANs Eircom would be the sole operator that was in fact able to rollout broadband.

In *MAN*, the Commission supported the Irish initiative to bridge the digital divide through public funding. It was established that the situation was characterised by a certain form of market failure:

*“As evidence in all European markets shows, the historic operators with market power in ‘traditional’ services such as telephony also had first mover advantages by offering broadband to their existing clients, thereby leveraging their market power into a new market. These characteristics of the sector and the previous existence of a state monopoly have led to market failure in the form of market power by Eircom in a number of markets.”*¹⁰⁷

The Swedish Incumbent TeliaSonera can be described as being one of those “historic operators” mentioned by the Commission in *MAN*. Through their former position as a State monopoly, with an existing network of customers through their own infrastructure, they have been able to shift their market power into a new market. From the Decision in *MAN*, this is the kind of situation in which the Commission admits the existence of a market failure that can justify granting of State aid in order to come to terms with the problem.

It seems like the Swedish model for granting State aid to projects concerning the deployment of broadband is well-designed in relation to the situation on the Swedish market. As shown in the Commission’s Decisions, State aid can be appropriate in situation similar to the Swedish one. It has the right incentive effects as there is no crowding-out of private initiative. The market has shown to be willing to contribute with at least 29% of the costs for broadband rollout. The Swedish model is proportional in the sense that aid measures are kept to a minimum since public procurement, which is generally accepted as a factor that keeps public funding to a minimum, is mandatory.

¹⁰⁶ Incumbents are usually former State monopolies that have been government agencies. These agencies have had responsibility for both monitoring the market as well as operating on it.

¹⁰⁷ C(2006)436 final, paragraphs 62-63.

3.2.3 Are the Potential Distortions of Competition Limited?

Regarding distortions of competition and effects on trade between Member States, the Swedish model seems to tackle these issues in an acceptable manner. The effect on trade should be limited, as foreign operators are rather encouraged than discouraged to establish themselves on the Swedish market. Without publicly funded broadband rollout, there would be no infrastructure available to foreign operators over which they could provide services to consumers.

Given the indicators that the Commission has named as pointing towards a compatible aid regime, the Swedish model fulfils the following:

- the funding concerns regions that are underserved,
- the regions concerned are commercially unattractive,
- an open tender procedure according to Community rules on public procurement is used to select a service provider,
- the constructed infrastructure is open to other operators.¹⁰⁸

On an overall balance, the Swedish model for granting State aid to projects concerning the deployment of broadband infrastructure seems to be acceptable on Community level.

3.3 What Local and Regional Authorities Can/Should Do

“Deployment of open access infrastructure, defined according to technological neutrality and managed by an independent entity, appears to be the solution most conducive to effective competition.”¹⁰⁹

Through its policies, the Commission strongly recommends governments to establish strategies for deployment of ICT infrastructure for broadband using the Structural Funds. This standpoint is clearly in line with the actions of the Swedish government, as Structural Funds have been used to a higher extent than expected.¹¹⁰

Local and regional authorities that want to grant State aid to projects concerning the broadband rollout can continue to follow the Swedish policy model. An assessment like the one the Commission would make in a similar situation can be made by the authorities. First, the common objective needs to be established. This is easily done, as broadband access is a highly valued

¹⁰⁸ Mechanisms to avoid over-compensation, technological neutrality, accounting transparency and the limitations of the funding has not been more closely examined in this thesis, but nothing points towards these factors *not* being present in the Swedish model.

¹⁰⁹ *Bridging the Broadband gap*, p. 9.

¹¹⁰ *Bredbandsutbyggnad med statligt stöd December 2006*, p. 37.

Community objective, but in this context it can be important to note which kind of infrastructure projects the authorities want to stimulate. The infrastructure must provide enough capacity for the transmission of necessary public services, and it must be flexible enough to cope with foreseeable future demands. Second, a thorough market analysis needs to be made in order to determine whether a market failure exists. This assessment can preferably be made by local and regional authorities, having the necessary knowledge of local and regional market conditions. Authorities are however advised not to act where it is not clearly necessary, and any unsound market developments that might follow from the established infrastructure must be examined beforehand and avoided.

Björn Björk, national expert on Information Technology Strategies at the Swedish Association of Local Authorities and Regions, makes the assessment that more State aid is needed to achieve the i2010 objectives. Market forces alone will not be able to achieve these goals, and since there is no documented discrimination of operators (i.e. distortion of competition) in regions where State aid *has* been used to finance infrastructure, State aid seems to be a good method to achieve the goals of i2010.¹¹¹ The distortions that do occur on the Swedish markets take place in regions where the infrastructure has only one owner, who simultaneously functions as operator of the infrastructure. Local and regional authorities should continue to use State aid in similar projects, and they should likewise apply for Structural Funds.

3.3.1 Public Procurement

The ECJ views public procurement as a reliable system, which creates compatibility safeguards towards the EC State aid rules.¹¹² The usage of an open, transparent and non-discriminatory public procurement procedure in an infrastructure project can lead to a measure not being considered as State aid at all, or that the State aid given to the undertaking chosen through an open tender procedure is compatible with the Common Market. However, if the project concerns an SGEI, the *Altmark* conditions also have to be satisfied in order to avoid the obligation to notify the Commission.¹¹³ The Commission is currently working on clarifying and simplifying the EC rules on public procurement.¹¹⁴

Even if the above stated renders public procurement “safe to use” by public authorities, scholars have adopted different views on what the implications of the ECJ judgment in *Altmark* are. According to Biondi et al, an important result of the case is that the ECJ clearly stated that the best policy of allocation of PSO is by using an open bid procedure, i.e. through a public procurement process.¹¹⁵ Bovis on the other hand implies that the ECJ and

¹¹¹ Interview with Björn Björk, 17 March 2007.

¹¹² Bovis, p.1.

¹¹³ Koenig & Kiefer, p. 416.

¹¹⁴ *White Paper on services of general interest*, p. 15-16.

¹¹⁵ Biondi, Eeckhout & Flynn, p. xv-xvi.

the CFI have developed diverging jurisprudence on the issue of State aid to projects financing SGEI. In his view, the European Courts have used different approaches to assess whether the funding of PSO, SGEI and services for the public at large can be regarded as State aid. The role of public procurement is slightly different in these approaches. Under the **State aids and compensation approaches**, public procurement “cleanses” public funding, which will be regarded as legitimate contributions for the provision of PSO and SGEI. From **procedural and substantive approaches**, the utilisation of public procurement exposes a necessary link without which the financing of public services is considered to be State aid. *Altmark* followed an ambiguous **hybrid approach** of the two. Bovis argues that the first *Altmark* criterion runs consistently with Art 86(2) EC jurisprudence, where an express act of the public authority to assign SGEI interest is required. The second criterion, however, departs from previous case-law as it establishes an *ex post* control mechanism. Regarding the third criterion, it is unclear whether the compensation for PSO may include a profit element. In addition, the fourth criterion inserts elements of subjectivity and uncertainty when there is no public procurement procedure, since a comparison then should be made between the recipient and a well-run private undertaking.¹¹⁶

There are two main methods to address market failure. One of them is to use regulation in order to come to terms with the problem. To monitor broadband deployment strictly through regulation would be to use a blunt and clumsy tool, especially since rapid and disruptive technological development changes the preconditions. Regulation in this field is quickly outdated, and it risks not being adhered to or applied in a counterproductive way. The other alternative to address market failure is to use market mechanisms to create commercial incentives that stimulate efficient competition. On a commercial basis, public procurement can be used both in order to maintain competition and to be able to set demands for the prospected infrastructure in terms of openness etc. Through market mechanisms, deals can be struck on a commercial level which would decisively benefit the Common Market more than regulation.¹¹⁷

3.3.2 Broadband as a SGEI

The improved status of SGEI within the Community legal framework can be traced through a number of Community documents. The Commission’s *White Paper on services of general interest*, its Notice on SGI,¹¹⁸ the case-law of *Altmark* and *Ferring* and the Commission’s Decisions in *MAN*, *ScA* and *Cumbria* are all landmarks that show the development of the status of SGEI within the Community framework. These documents provide the basis

¹¹⁶ Bovis, pp. 25-27.

¹¹⁷ Interview with Björn Björk, 17 March 2007. At the conference *Bridging the Broadband Gap*, Brussels 14-15 May 2007, this was strongly highlighted by Viviane Reding, Commissioner for Information Society and Media. Interview with Björn Björk, 18 May 2007.

¹¹⁸ Kommissionens Meddelande, *Tjänster i allmänhetens intresse i Europa*, KOM(2000) 580 slutlig.

for why SGEI are considered to be so important in the Community. The mentioned Decisions indicate that broadband can be seen as an SGEI. Other Decisions strengthen this position.¹¹⁹

An updated Notice on SGI was supposed to be published in December 2006, but this has been delayed for some reason. This document will, when published, be able to shed some light on the issue of whether broadband should be seen as a SGEI.

3.3.3 Broadband as a USO

The USO Directive is up for review during 2007, and it has been argued that broadband should be included in the refined concept of a USO. The argument is that since the market is constantly changing, the definition of what is included in the term USO needs to change with the rest of society. Providing consumers with fixed telephony used to be what the market could not achieve by itself. Today, broadband access is rather the issue. In Sweden, the **Significant Market Power (SMP)** within the sector, TeliaSonera, has even been relieved of its duty to perform USO's. The market is deemed competitive and capable enough to provide fixed telephony to consumers.¹²⁰

In any case, to define USO's as to include broadband is a political issue of Competition law – not a legal matter. It remains to be seen which shape the new USO Directive will take after the review. Sweden can try to influence the draft so that access to broadband is included in the updated USO definition. PTS recommends the Swedish government to actively strive for this.¹²¹ The Swedish definition of USO's is ultimately controlled by the EC definition in the USO Directive, but the Member States are allowed to expand the definition according to national needs. The Swedish legislator can therefore, regardless of change in the USO Directive, decide to include broadband in the Swedish definition of USO's.

¹¹⁹ See note 85. For a further discussion on broadband as SGEI, see Anestis, Mavroghenis & Psaraki.

¹²⁰ This view comes from a judgment in Länsrätten (The County Administrative Court) of Stockholm, 5th of February 2007. Mål nr 20346-05, Länsrätten i Stockholms län, *TeliaSonera vs Post- och Telestyrelsen*. The status and importance of electronic communications in Sweden has its roots in the Telelag (1993:597) and Radiolag (1966:755), which were merged into the LEK in 2003. Electronic communications was considered to be a USO already from the start, but only telephony was included in the Swedish legal concept of USO's that had to be provided by TeliaSonera.

¹²¹ *Förslag till bredbandsstrategi för Sverige*, p. 4.

4 Analysis

This chapter will make a coherent analysis of the current legislation and analyse possible solutions to the thesis questions.

The Swedish policy regime for granting State aid to broadband deployment is modelled after the Treaty Articles on non-discrimination and transparency (Articles 43 and 49 EC). It advocates public procurement as the way to appoint aid beneficiaries, and the established infrastructure or networks must be kept open to other operators or service providers. Only rural areas are eligible for State aid, and it is only the regional or local networks that are eligible – not projects concerning the national backbone or the local loop.

A flaw in the Swedish regime is that it was never notified to the Commission, but it has nevertheless been in use since 2001.¹²² A new regime is currently being discussed, which is based on the previous model. The problem is that the Commission has the exclusive right to establish that a specific State aid regime *is* compatible with EC law – this is not left to the discretion of the Member States.¹²³ If the Commission should decide to acknowledge that the Swedish model is unlawful, a problem of repayment might arise. State aid granted according to incompatible rules has to be repaid, but this might turn out to be impossible. There is presently no Swedish law that allows retroactive repayment of granted State aid, and some companies might go bankrupt if they are forced to pay back investments that were crucial for them in their infrastructure projects.¹²⁴

One reason why the Swedish policy on State aid to broadband was never notified to the Commission was that there were no predecessors. No other country had notified, or even developed, their models. At the time when the policy was conceived, the Community State aid rules could be interpreted as allowing public funds to be used if necessary, as long as the funding did not distort competition. Another reason was that there was a hurry to initiate the rollout of broadband infrastructure, in order to meet the political objectives of e2005 and i2010. The market failure regarding broadband deployment in rural areas was apparent, and for that reason a model that allowed local authorities to obtain State aid, if they used public procurement as a method to initiate infrastructural projects that would result in open networks, was quickly put into effect. Monopolies were not allowed, and the local authorities were only allowed to run the infrastructure by themselves if they did not receive acceptable bids in the open tender procedure. Statistics show

¹²² The case concerns a new unnotified aid, constructed and put into force *after* the Swedish EU accession.

¹²³ National courts are however allowed to establish that a regime is *not* compatible with EC law.

¹²⁴ A law concerning retroactive repayment of incompatible State aids is, however, in the process of being drafted. Small companies, which were dependent on State aid for their engagement in the deployment of broadband infrastructure, might nevertheless go bankrupt if they are forced to repay this funding.

that these rules were adhered to. Where State aid has been granted, the infrastructure has been open for all operators and there is no distortion on these markets. In regions where State aid has not been granted however, distortion has occurred either due to private operators, who own the infrastructure and can maintain a monopoly status, or due to local authorities that have instigated broadband projects on their own without any governmental support.¹²⁵

Despite the failure to notify the Commission, there is in my assessment a low risk that the Commission should deem the Swedish model for granting State aid to broadband deployment as incompatible with EC law. Even if the aid granted is by definition unlawful, it only has to be recovered from the beneficiaries if it is considered *incompatible with the Common market*. The Swedish regime has been in force since 2001, and regularly conducted surveys made by SKL, PTS and Länsstyrelserna clearly indicate that there is no distortion of competition on markets where State aid has been involved. On these markets, the principles established by the Commission (described above in Chapter 2.3.1.3) seem to have been upheld – especially those of proportionality and non-distortion of competition.

Problems have however occurred where private operators have financed rollout on their own, without the aid of public funding. These operators are in a position where they can deny other operators access to their privately owned infrastructure. This behaviour clearly distorts competition. Even if the Swedish regime was never formally notified, the Commission is by no means ignorant of the situation in Sweden. The system that has been put into use cannot have escaped the eyes-and-ears of the Commission. Sweden has even been referred to as a model Member State for its achievements in this field.¹²⁶

The Commission has adopted the position that where the typical rules of the risk capital market will hinder development, “*the State is sometimes the only actor able to change the incentives for investors, to make them consider innovative ventures worth a try.*”¹²⁷ A possible solution to the problem of a lack of risk capital would be if the public (i.e. the state,

¹²⁵ Interviews with Ellen Hausel-Heldahl, Legal Adviser at the Ministry of Enterprise, Energy and Communications, 15 March 2007 and Björn Björk, 17 March 2007. See also *Bredbandsutbyggnad med statligt stöd December 2006*.

¹²⁶ Besides, why should the Commission spend time and energy working against a State aid regime that successfully promotes an important Community objective? The Swedish fear of disclosure is unmotivated – a deal could be made with the Commission about how to come to terms with the unlawfulness of the aid regime. Theoretically, the Commission could make an adjustment of possible repayment of incompatible aid, but this scenario is highly unlikely in my opinion as the aid granted in accordance with the Swedish model should be deemed compatible. The Commissioner for Regional Policy, Danuta Hübner, even named the Swedish broadband project “*an encouraging success story*” and a model example to other countries at the conference *Bridging the Broadband Gap, Brussels 14-15 May 2007*. Interview with Björn Björk, 18 May 2007. The whole issue stems from a bureaucratic mistake, and however important it might be it is not the end of the world.

¹²⁷ Neelie Kroes, Speech/05/440: *The State Aid Action Plan – Delivering Less and Better Targeted Aid*.

government or authorities of any kind) could offer operators the loans they need for projects concerning deployment of broadband infrastructure. In this way, tax money could be used to finance the rollout. The problem of scarce risk capital would be addressed on a political level, and the demands for reimbursement could be lowered through the conditions of usage of the public funds.

France has in fact implemented a similar model. The French **Caisse des Dépôts (CDC)** “*is a state-owned financial institution that performs public-interest missions on behalf of French central, regional and local authorities.*”¹²⁸ CDC co-invests in areas where market failure cause projects to receive insufficient funding, and it promotes the development of PPP’s.¹²⁹ Among many other things, CDC support local and regional digital infrastructure projects by giving long-term loans to projects concerning primary broadband infrastructure.¹³⁰ The French model includes a clear requirement for openness of the established infrastructure, and the Commission has not complained about this system.

Another way to make public funding of broadband deployment legitimate in every situation is for the Commission to include this kind of State aid under a block exemption, as has been done with other kinds of aid that have been considered to support public interest issues. In this case, aid measures with the objective of supporting broadband deployment in rural areas would not have to be notified. A possible reason why State aid to broadband deployment should be exempted could be because it is not considered as the most distortive type of aid, but this view could easily be contested.

4.1 The Development of the State Aid Regime

Legislation is difficult in relation to the issue of granting State aid to broadband deployment. Technological convergence causes a rapid and disruptive change of technical preconditions, which causes recently adopted laws or regulations to become obsolete, almost before they were put into use, unless the legislation uses flexible concepts that focus on the achievement of set objectives instead of being technically detailed and precise. A strictly legal perspective on State aid law seems counterproductive in this policy field.

¹²⁸ Quote from CDC’s homepage,
http://www.caissedesdepots.fr/spip.php?page=sommaire_gb.

¹²⁹ Caisse des Dépôts Annual Report 2005, *Long-term management in the service of France*, available at <http://www.caissedesdepots.fr/spip.php?article59>.

¹³⁰ <http://www.caissedesdepots.fr/spip.php?article93>. In 2003, more than 100 such projects were in process. French law allows local authorities to establish infrastructure, but they are not allowed to act as telecommunications operators themselves. See *A Survey of Local Development of Telecommunications Infrastructure across Europe*, published by Corning, p.2, available at <http://www.corning.com/search/results.aspx?n=Meni%20Styliadou&scope=/>.

Since 1999, the two biggest developments in the area of State aid control have been the launching of the SAAP and the introduction of economic analysis. In this context, it is interesting to compare the Commission's Decisions on broadband deployment projects,¹³¹ especially *MAN*, with its Decision on State aid to digital terrestrial TV in Berlin-Brandenburg (hereafter referred to as *Digital TV Berlin*).¹³² In *Digital TV Berlin*, a well-defined objective of common interest was pursued – the digital switchover – and several market failures could be noted. Nevertheless, granting State aid to private broadcasters was considered incompatible with the Common market, mainly for economic reasons. The overall market analysis showed a strong distortion of competition of digital TV vis-à-vis other technological platforms (cable, satellite and broadband). State aid to private broadcasters was deemed neither necessary nor appropriate to achieve the important objective of digital switchover. In *MAN*, a well-defined objective of common interest was pursued – broadband deployment – and a market failure was evident. State aid was seen as an appropriate instrument to come to terms with the market failure, as other investigated measures proved to be insufficient. The overall balance of the measure, the market analysis, was positive because the aid was kept to a minimum, the process of open tender was used, the infrastructure was publicly owned, crowding-out effects were limited as well as the effect on trade etc.¹³³ It was economic aspects that tipped the scale, not legal ones.

In its Decisions on public funding to broadband projects, the Commission views economic parameters from a competition law perspective, and not from a strict legal perspective. What the Commission basically says is that the measures at issue in each case are maybe not compatible with the *Treaty provisions*, but they are compatible with *EC law* because of the economic aspects. Before turning to Article 87 EC, it needs to be established whether Article 86(2) EC can be used. This means that economic aspects and consequences are given weight, and it has not been common to do so in the area of Community State aid law. There is however a trend in Community law to use economic analysis rather than make a strict legal assessment.

There is a question of whether economic analysis in the field of State aid control will lead to a stricter approach, in the sense that the rules will become more coherent. A refined economic analysis, i.e. the basic tests under Article 87(3)c (whether a State aid measure is necessary and proportional), is inherent in a refined economic approach. A refined economic approach may not be a revolution, but it helps to systemise the analysis, clarify the specific problems a State tries to tackle (with the use of State aid) and is capable of taking the actual market situation into account. It

¹³¹ See Chapter 2.3.1.3, in particular note 85.

¹³² Commission Decision C(2005)3903 of 9 November 2005 *on the State Aid which the Federal Republic of Germany has implemented for the introduction of digital terrestrial television (DVB-T) in Berlin-Brandenburg*. See also Loretta Dormal Marino, *College of Europe Global Competition Law center 3rd Annual Conference Brussels 21-22 September 2006*.

¹³³ *Ibid.*

is also capable of increasing the transparency and predictability of methods of State aid law. The approach may help Member States to better design their measures, and increasing effectiveness and efficiency it can facilitate reaching the Community goal of less and better targeted State aid.¹³⁴ So far, there are however no Commission Guidelines with relevance for cases examined directly under Article 87(3)c EC.

There has been a great debate on whether economic analysis should be used in State aid law, but the Commission has adopted this method both in the SAAP, which promotes a refined economics-based approach, and in its recent decisions of *MAN*, *Cumbria* and *Scottish Aggregated*.¹³⁵ The discussion seems to be settled through this,¹³⁶ but it is ultimately up to the European Courts to resolve it once and for all. Their assessment is still to be made.

In my opinion, an economic approach to the issue of compatibility of State aid to broadband deployment is able to solve problems that a strict legal approach is forced to overlook. Rules concerning the Common Market must be flexible in order to follow the constant changes of society and Community policy, otherwise they will create more problems than they are able to solve.

In relation to the question of whether or not economic analysis should be used, is the question of which Community objective should be given more weight – the objective of State aid control or the i2010 objective of broadband to all. Is it possible to stretch the general prohibition on State aid as to exclude measures that promote the i2010 objective? Where should the line be drawn in that case – can other Community objectives also outweigh the core of State aid law – the general prohibition? The latter question may be too wide to be included in the scope of this thesis, but the previous question can easily be answered. It is in my opinion clear from the Commission's policy that it is much more important to achieve the i2010 objective than to uphold the general prohibition on State aid. The consequences of this consideration, in terms of economic growth and social cohesion, are much more beneficial to the prosperity of the Common Market than the alternative. In light of the second question, it can however be important to point out once more that it is only broadband deployment in

¹³⁴ Ibid.

¹³⁵ In C(2003)4489 final, *Cumbria Broadband – Project Access – Advancing Communication for Cumbria and Enabling Sustainable Services*, the purpose of the contested rollout was for schools and educational institutions in a rural area to get broadband access. These objectives were seen as valid to justify State aid to broadband deployment, especially since there was no commercial operator present on the market. In C(2005)2720 final, *Aggregated public sector procurement of broadband in Scotland*, the Commission conducted a similar discourse. Considering an existing market failure, it was ok to grant State aid to support the provision of a SGEI. Defining a measure as a SGEI had no meaning or consequence until it was notified to the Commission, but in that context it should be notified according to Article 86(2) EC instead of Article 87 EC.

¹³⁶ Hancher, Ottervanger & Slot however, disagree. They argue that a Competition-based analysis is not well developed in the field of State aid law. Hancher, Ottervanger & Slot, p. 33.

rural (or “less-developed”) areas that are at issue – developed regions are considered capable of achieving broadband rollout without State intervention.

4.2 Service vs Infrastructure, and Separation of Functions

One problem connected with the issue of broadband deployment is that broadband traditionally has been defined as a commodity – not as a type of infrastructure similar to roads, water, energy etc. Whether you analyse broadband as a commodity or as infrastructure (that might be considered a SGEI) will produce different assessments. Rural areas may for example generally accept lower levels of offered commodities than of public services. This is because the geographic and demographic set up of a rural area should reasonably entail an acceptance of lower levels of commodities, but it cannot accept lower levels of public services. Basic infrastructure, access to health care and education etc must be offered in these areas – otherwise they risk being worse off than, and excluded from, the rest of society.

The Commission notes in the *State Aid Action Plan* that “[t]he Lisbon Action Plan stresses that modern transport, energy and information and communication technology infrastructures throughout the EU territory are a prerequisite for reaping the benefits of a re-invigorated Lisbon Strategy.”¹³⁷ This statement can be seen as support for the estimation that ICT should be regarded as infrastructure, and not as a service.

Closely linked to the question of whether broadband should be seen as a commodity or as infrastructure is the issue of separation of functions. There might very well be a conflict of interest between the owner of infrastructure and the provider of services over the same infrastructure, especially when one operator is able to own infrastructure and allow other operators access only to a limited extent or at higher prices (as is happening with the Swedish Incumbent TeliaSonera). As noted above in 3.2.1, TeliaSonera’s behaviour has created market barriers.

PTS suggests that the barriers on the Swedish market can be removed with a new model for equal treatment. They suggest that TeliaSonera should be functionally separated, as has been done with British Telecom (BT). In the British model, called openreach, the wholesale organisation is separated from the rest of the company. BT has to provide wholesale products on equal terms to its own retail operations as well as its competitors. PTS recommends the Swedish State, as the main shareholder in TeliaSonera, to act in order to make the company go through with a functional

¹³⁷ *State Aid Action Plan*, paragraph 47.

separation.¹³⁸ The suggested separation of functions is supported by the openreach model as well as the Commission.¹³⁹

I believe that broadband regulation needs to be more closely linked to the rules concerning traditional infrastructure such as roads, water and energy. Electronic communications are one of the main pillars of today's information society, and broadband, as a means of electronic communications, should consequently be regarded as one of its most fundamental infrastructures. As PTS suggests, the broadband market should be separated into owners of *infrastructure and carrier services*,¹⁴⁰ and operators/providers of *content services* (i.e. commodities) over the constructed infrastructure. The creation and maintenance of the costly broadband *infrastructure* could then be the responsibility of the State, and the market could take care of the provision of *content services*. In my opinion, it should be the responsibility of the State to act where there is a market failure of providing broadband infrastructure. Granting State aid in order to establish open networks that are accessible to all operators on equal terms, Member States can actively lower entry barriers for all operators providing content services to consumers.

My last remark is that the Commission pointed out in *MAN* that there is also a possible conflict of interest when the State is active both as an infrastructure owner and as a regulatory authority. In one of their Guidelines,¹⁴¹ the Commission points out that the principles of transparency and non-discrimination must be respected and upheld in such situations. In *MAN*, the Irish authorities argued that the different roles of the public authorities were completely separated, and thus the possible conflict of interest was avoided.¹⁴² This possible conflict of interest is an interesting issue that needs to be examined further, but there is unfortunately no space to research this in the present thesis.

¹³⁸ *Förslag till bredbandsstrategi för Sverige*, pp. 5-6. For more information on openreach, visit <http://www.openreach.co.uk/orpg/home/home.do>. In response to the market's criticism, TeliaSonera recently decided to allow all other operators access to the PSTN. This is however not a functional separation, and it remains to be seen how TeliaSonera's change in policy will affect the market situation. DN Debatt, 3 May 2007, article available at <http://www.dn.se/DNet/jsp/polopoly.jsp?d=572&a=640301>.

¹³⁹ Commissioner Viviane Reding recommended functional separation at the conference *Bridging the Broadband Gap, Brussels 14-15 May 2007*. Interview with Björn Björk, 18 May 2007.

¹⁴⁰ **Carrier services** are electronic services that ensure transmission of data signals over the network, as opposed to **content services** that consist of the actual services offered over the infrastructure.

¹⁴¹ *Guidelines on criteria and modalities of implementation of structural funds in support of electronic communications*.

¹⁴² C(2006)436 final, paragraph 82.

5 Conclusion

*“The [reform of European State aid policy] cannot be successful without clear support from all stakeholders, and in particular from Member States and regional and local aid granting authorities. State aid reform will only work if we all but into it.”*¹⁴³

The area of State aid law has previously been known for its lack of accessibility, transparency and consistency. The area has in general been overlooked by legal scholars and commentators. Today, these factors have largely improved thanks to electronic access to the Decisions of the Commission, websites with State aid registers and weekly electronic newsletters.¹⁴⁴ More and more books and articles are published on the subject, and the case-law has expanded – even if it has not settled yet. Nevertheless, the policy on State aid in the context of SGEI and broadband deployment is characterised by its inconsistency. There is not yet any case-law on this particular type of State aid, and even if the Commission’s Decisions tend to uphold a consistent view on the matter, the circumstances in each different case has to be examined. The multitude of Guidelines, Frameworks, White Papers and Decisions that the Commission has published over the years provide a diffuse legal area which is difficult to penetrate. No wonder that the Swedish government never notified their State aid model to the Commission – at the time it did not seem necessary as long as the requirements of prevailing State aid law were upheld.

When it comes to deploying broadband infrastructure, the ability of local and regional authorities to act is strongly dependent on national policies. It is however clear from the research in this thesis that local communities can facilitate investment in basic infrastructure by sharing the costs of the deployment, and this can even enhance competition for services and promote local broadband development.¹⁴⁵

This thesis shows that the Commission has developed a policy on State aid to broadband deployment that follows the main principles of the European Courts’ case-law – even if that case-law has turned out to be ambiguous in itself.¹⁴⁶ Be that as it may, the Commission’s policy has not yet been assessed by the European Courts, and it is presently impossible to tell how the CFI and the ECJ will address the issue. At the moment, Member States can nevertheless look to the practice of the Commission. Even if the specific circumstances in an individual case might lead to a different conclusion,

¹⁴³ Neelie Kroes, Speech/05/440: *The State Aid Action Plan – Delivering Less and Better Targeted Aid*.

¹⁴⁴ Hancher, Ottervanger & Slot, pp. 4-5.

¹⁴⁵ See *A Survey of Local Development of Telecommunications Infrastructure across Europe*.

¹⁴⁶ See Chapter 3.3.1.

measures granting funds to projects promoting the deployment of broadband infrastructure is generally compatible with EC law if a combination of the following indicators are present:

- the measure concerns regions that are less-developed;
- the measure concern regions that are commercially unattractive;
- an open tender procedure, according to the Community rules on public procurement, has been used in choosing a service provider;
- mechanisms to avoid over-compensation are present;
- competitors are allowed equal access to the established infrastructure;
- the project is technologically neutral;
- granted funds are put into separate accounts; and
- the amount and duration of the funding is limited.

In my opinion, shared by Hencsey et al, public intervention in the area of broadband deployment may result in the establishment of necessary infrastructure, while ensuring at the same time that competition is upheld by enforcing open access requirements for the equipment installed.¹⁴⁷

An important conclusion to be drawn from this thesis is that the sector of electronic communications is in constant motion, as technologic developments that change the preconditions are invented practically daily. A market characterised by such rapid and disruptive change needs a legislative framework that is flexible and capable of adapting itself to different technological preconditions, depending on whatever is currently à jour, without getting obsolete. Legislation must be allowed to be managed by objectives, and not designed in terms of detailed, rigid laws.

The Commission's present policy signals a new direction for the position of State aid in the Community. State aid has traditionally been granted by Member States to State owned enterprises, in order to help them perform better and hopefully hinder other businesses from entering the market. Designed in this fashion, State aid is clearly incompatible with the objectives of the Common Market – especially with the idea that market forces alone should be allowed to regulate the functioning of the market.

Today's generation of State aid is rather targeted at neutralising market failures, wherever they occur. Using State aid in order to fulfil important Community objectives, the Commission has proven itself willing to look to the consequences for the citizens of the EU rather than dismissing the possibility State aid has to offer as incompatible with the Common Market. Compared to how State aid used to function, this is a new way of looking at public intervention on the market. A similar change has occurred in Community Competition law, where legal solutions have transformed from imposing strict prohibitions to allowing rule of reason to prevail. Modern Competition law is more focused on economic consequences, as economic

¹⁴⁷ Hencsey et al, p. 9.

analysis has become standard within this field of law. It seems like State aid law will follow this development.

During the course of my work, I have encountered several issues that would need further examination. Suggested further studies would be to look at one or several of the following questions:

- Are the principles of transparency and non-discrimination respected and upheld when a Member State is active both as an infrastructure owner and as a regulatory authority? Examine the possible conflict of interest.
- What possibilities do private operators have when there is a market failure? Some operators have been active in deploying wireless networks when local authorities have proven unwilling to deploy fibre, how do this infrastructure function in relation to Community objectives of sustainable technology?
- How will the position of economic analysis develop in relation to State aid law?
- Do the markets for deployment of fibre vs copper wire produce different complications? What will happen with the PSTN now that TeliaSonera has been relieved of their USO?
- Does the sector of electronic communications need to be specifically regulated, or could regular Community Competition law ensure the policy objectives for broadband deployment? If special regulation is needed at the moment, is it possible that this will change in the near future?

Finally, EU's regulatory framework for eCommunications has been under review since 2005. In the summer of 2007, a proposal to modify the present framework will reach the European Parliament, and the new framework is expected to be in force by 2009-2010.¹⁴⁸ It remains to be seen whether this framework will change the Commission's policy on State aid to broadband deployment.

¹⁴⁸ http://ec.europa.eu/information_society/policy/ecommm/tomorrow/roadmap/index_en.htm

Supplement A – Relevant Treaty Articles¹⁴⁹

Article 16 EC

“Without prejudice to Articles 73, 86 and 87, and given the place occupied by services of general economic interest in the shared values of the Union as well as their role in promoting social and territorial cohesion, the Community and the Member States, each within their respective powers and within the scope of application of this Treaty, shall take care that such services operate on the basis of principles and conditions which enable them to fulfil their missions”.

Article 86 EC

“1. In the case of public undertakings to which Member States grant special or exclusive rights, Member States shall neither enact nor maintain in force any measure contrary to the rules contained in this Treaty, in particular to those rules provided for in Article 12 and Article 81 to 89.

2. Undertakings entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly shall be subject to the rules contained in this Treaty, in particular to the rules on competition, in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Community.

3. The Commission shall ensure the application of the provision of this Article and shall, where necessary, address appropriate directives or decisions to Member States.”

Article 87 EC

“1. Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market.

¹⁴⁹ Source: European Union Consolidated Versions of the Treaty on European Union and of the Treaty Establishing the European Community, Official Journal C 321 E/1.

2. *The following shall be compatible with the common market:*

- (a) *aid having a social character, granted to individual consumers, provided that such aid is granted without discrimination related to the origin of the products concerned;*
- (b) *aid to make good the damage caused by natural disasters or exceptional occurrences;*
- (c) *aid granted to the economy of certain areas of the Federal Republic of Germany affected by the division of Germany, in so far as such aid is required in order to compensate for the economic disadvantages caused by that division.*

3. *The following may be considered to be compatible with the common market:*

- (a) *aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underdeployment;*
- (b) *aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State;*
- (c) *aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest;*
- (d) *aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest;*
- (e) *such other categories of aid as may be specified by decision of the Council acting by a qualified majority on a proposal from the Commission.”*

Article 88 EC

1. *The Commission shall, in cooperation with Member States, keep under constant review all systems of aid existing in those States. It shall propose to the latter any appropriate measures required by the progressive development or by the functioning of the common market.*

2. *If, after giving notice to the parties concerned to submit their comments, the Commission finds that aid granted by a State or through State resources is not compatible with the common market having regard to Article 87, or that such aid is being misused, it shall decide that the State concerned shall abolish or alter such aid within a period of time to be determined by the Commission.*

If the State concerned does not comply with this decision within the prescribed time, the Commission or any other interested State may, in derogation from the provisions of Articles 226 and 227, refer the matter to the Court of justice direct.

On application by a Member State, the Council may, acting unanimously, decide that aid which that State is granting or intends to grant shall be considered to be compatible with the common market, in derogation from the provisions of Article 87 or from the regulations provided for in Article 89, if such a decision is justified by exceptional circumstances. If, as regards the aid in question, the Commission has already initiated the procedure provided for in the first subparagraph of this paragraph, the fact that the State concerned has made its application to the Council shall have the effect of suspending that procedure until the Council has made its attitude known.

If, however, the Council has not made its attitude known within three months of the said application being made, the Commission shall give its decision on the case.

3. *The Commission shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid. If it considers that any such plan is not compatible with the common market having regard to Article 87, it shall without delay initiate the procedure provided for in paragraph 2. The Member State concerned shall not put its proposed measures into effect until this procedure has resulted in a final decision.”*

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