OPINION OF ADVOCATE GENERAL GEELHOED

delivered on 7 June 2001 [1]

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I — Introduction

1. In this case the Commission of the European Communities seeks a declaration by the Court that the French Republic has failed to fulfil its obligations by

— failing to implement Article 4c of Commission Directive 90/388/EEC of 28 June 1990 on competition in the markets for telecommunications services, [2] as amended by Directive 96/19/EC, [3] and

1 — Original language: Dutch.

2 — OJ 1990 L 192, p. 10.
3 — OJ 1996 L 74, p. 13.

— failing to comply with Article 5(1), (3), (4) and (5) of Directive 97/33/EC of the European Parliament and of the Council of 30 June 1997 on interconnection in Telecommunications. [4]

The case relates to obligations connected with the provision of universal service in respect of voice telephony, [5] which is supplied in France by France Télécom.

II — Legal framework

European law

2. The universal service obligation for fixed voice telephony stems from Article 3 of Directive 95/62/EC of the European Parliament and of the Council of 13 December 1995 on the application of open network provision (ONP) to voice telephony, which provides as follows:

'Member States shall ensure that the respective telecommunications organisations separately or jointly provide a fixed public telephone network and a voice telephony service in accordance with the provisions of this directive, in order to guarantee a harmonised offering throughout the Community.

In particular Member States shall ensure that users can:

(a) obtain on request a connection to the fixed public telephone network;

(b) connect and use approved terminal equipment situated on the users' premises, in accordance with national and Community law.

...'

The term 'universal service provision' is not used in the directive. It is, however, in Directive 98/10/EC of the European Parliament and of the Council of 26 February 1998 on the application of open network provision (ONP) to voice telephony and on universal service for telecommunications in

4 — OJ 1997 L 199, p. 32.
5 — OJ 1995 L 321, p. 6.

a competitive environment. [6] This directive stipulates which services universal service provision must always include. They are connection to the fixed public telephone network, directory services and public pay telephones.

3. Directive 96/19 incorporated into Directive 90/388 a new Article 4c, which reads as follows:

'Without prejudice to the harmonisation by the European Parliament and the Council in the framework of ONP, any national scheme which is necessary to share the net cost of the provision of universal service obligations entrusted to the telecommunications organisations with other organisations, whether it consists of a system of supplementary charges or a universal service fund, shall:

(a) apply only to undertakings providing public telecommunications networks;

(b) allocate the respective burden to each undertaking according to objective and non-discriminatory criteria and in accordance with the principle of proportionality.

Member States shall communicate any such scheme to the Commission so that it can verify the scheme's compatibility with the Treaty.

Member States shall allow their telecommunications organisations to re-balance tariffs taking account of specific market conditions and of the need to ensure the affordability of a universal service, and, in particular, Member States shall allow them to adapt current rates which are not in line with costs and which increase the burden of universal service provision, in order to achieve tariffs based on real costs. Where such rebalancing cannot be completed before 1 January 1998 the Member States concerned shall report to the Commission on the future phasing out of the remaining tariff imbalances. This shall include a detailed timetable for implementation.

...'

4. Under Article 2 of Directive 96/19, 'Member States shall supply to the Commission, not later than nine months after the directive has entered into force, such information as will allow the Commission to confirm that points 1 to 8 [7] of Article 1 are complied with.' The directive entered into force on 11 April 1996. The period within which that information had to be supplied therefore elapsed on 11 January 1997.

6 — OJ 1998 L 101, p. 24.

7 — Article 4c was incorporated by Article 1(6) of Directive 96/19.

5. Article 5 of Directive 97/33 relates to interconnection and contributions to the universal service. It provides that:

'1. Where a Member State determines, in accordance with the provisions of this article, that universal service obligations represent an unfair burden on an organisation, it shall establish a mechanism for sharing the net cost of the universal service obligations with other organisations operating public telecommunications networks and/or publicly available voice telephony services. Member States shall take due account of the principles of transparency, non-discrimination and proportionality in setting the contributions to be made. Only public telecommunications networks and publicly available telecommunications services as set out in Part 1 of Annex I may be financed in this way.

2. Contributions to the cost of universal service obligations if any may be based on a mechanism specifically established for the purpose and administered by a body independent of the beneficiaries, and/or may take the form of a supplementary charge added to the interconnection charge.

3. In order to determine the burden if any which the provision of universal service represents, organisations with universal service obligations shall, at the request of their national regulatory authority, calculate the net cost of such obligations in accordance with Annex III. The calculation of the net cost of universal service obligations shall be audited by the national regulatory authority or another competent body, independent of the telecommunications organisation, and approved by the national regulatory authority. The results of the cost calculation and the conclusions of the audit shall be open to the public in accordance with Article 14(2).

4. Where justified on the basis of the net cost calculation referred to in paragraph 3, and taking into account the market benefit if any which accrues to an organisation that offers universal service, national regulatory authorities shall determine whether a mechanism for sharing the net cost of universal service obligations is justified.

5. Where a mechanism for sharing the net cost of universal service obligations as referred to in paragraph 4 is established, national regulatory authorities shall ensure that the principles for cost sharing, and details of the mechanism used, are open to public inspection in accordance with Article 14(2).

National regulatory authorities shall ensure that an annual report is published giving the calculated cost of universal service obligations, and identifying the contributions made by all the parties involved.

6. Until such time as the procedure described in paragraphs 3, 4 and 5 is implemented, any charges payable by an interconnected party which include or serve as a contribution to the cost of universal service obligations shall be notified, prior to their introduction, to the national regulatory authority. Without prejudice to Article 17 of this directive, where the national regulatory authority finds, on its own initiative, or after a substantiated request by an interested party, that such charges are excessive, the organisation concerned shall be required to reduce the relevant charges. Such reductions shall be applied retrospectively, from the date of introduction of the charges, but not before 1 January 1998.'

6. Annex III to the directive states how the costs of universal service obligations for voice telephony are to be calculated. It provides *inter alia* that the 'cost of universal service obligations shall be calculated as the difference between the net cost for an organisation of operating with the universal service obligations and operating without the universal service obligations.... The calculation shall be based upon the costs attributable to:

(i) elements of the identified services which can only be provided at a loss or provided under cost conditions falling outside normal commercial standards.

This category may include service elements such as access to emergency telephone services, provision of certain public pay telephones, provision of certain services or equipment for disabled people, etc.

(ii) specific end-users or groups of end-users who, taking into account the cost of providing the specified network and service, the revenue generated and any geographical averaging of prices imposed by the Member State, can only be served at a loss or under cost conditions falling outside normal commercial standards.

...

Revenues shall be taken into account in calculating the net cost. Costs and revenues should be forward-looking.'

French law

7. Under French telecommunications legislation, a system has existed in France since 1997 for sharing the net cost of universal service provision between the various telecommunications providers. The universal service is provided by France Télécom. The legislation was introduced on the basis of a 1996 report by a group of independent experts (the Champsaur report).

8. The provisions relevant to this case are Articles R 20-31 to R 20-34 of the Code des postes et télécommunications ('the Code'). Article R 20-31 provides that the net cost of universal service provision is made up of three components. These components are referred to as C1, C2 and C3. In respect of 1997 a decree of 13 May 1997 (No 97-475) provides for a flat-rate calculation of the total of the three components in anticipation of specific methods of calculation which will be applied for each of the three components in subsequent years. Articles R 20-32 to R 20-34 contain methods of calculation for the years after 1997. All those articles were incorporated into the Code by Law No 96-659 of 26 July 1996.

9. Finally, it should be noted that responsibility for supervising the telecommunications sector in France lies with the Autorité de régulation des télécommunications ('ART').

III — The pre-litigation procedure

10. By letter of 4 June 1997 the French authorities notified to the Commission Law No 96-659 of 26 July 1996 amending the Code, and certain implementing decrees, pursuant to Article 2 of Directive 96/19.

11. The Commission subsequently put a number of questions to the French Government by letter of 7 November 1997. The questions related to the timetable for balancing the tariff structure of France Télécom, the traditional telecommunications provider in France, and to the methods of calculating this tariff structure and the procedures for financing and calculating the net cost of the universal service. The French authorities responded by letter of 4 December 1997.

12. On the basis of this response the Commission concluded that France had failed to fulfil certain obligations under Directive 90/388, as amended by Directive 96/19, and Directive 97/33. By letter of 24 July 1998 the Commission served formal notice on the French Republic. The French Government responded by letter of 4 November 1998, to which it attached a draft decree relating to France Télécom's hardship rates. On 8 July 1999 the Com-

mission delivered a reasoned opinion. In its response of 3 December 1999, the French Government maintained its previous arguments. The application initiating these proceedings was then lodged with the Court.

IV — General remarks

13. The Commission's complaints in this case are directed at the way in which the rules on what is known as universal service in the telecommunications sector were implemented in France. Article 2(g) of Directive 97/33 defines universal service as follows: 'a defined minimum set of services of specified quality which is available to all users independent of their geographical location and, in the light of specific national conditions, at an affordable price'. In other words, the universal service obligation includes maintaining non-profitable telephone services, for example in sparsely populated areas. In France the universal service obligation lies with France Télécom. The Commission's complaints are directed at the way in which the cost of the universal service is calculated and the circumstances in which other telecommunications providers may be required to make a financial contribution to it.

14. Before dealing with the individual complaints, I would like to outline the context of this case by making certain preliminary remarks. In the 1990s the telecommunications sector was rapidly liberalised at Community level. Often detailed rules were necessary to ensure that newcomers would actually gain access to a market which had hitherto been controlled by nationally organised monopoly-holders. A characteristic feature of a large proportion of these rules, such as those relating to universal service, is that they impose obligations on the former monopoly-holders for the benefit of newcomers to the market.

15. The rules must ensure that former monopoly-holders charge only real costs to newcomers to the market where they avail themselves of their networks. This results in a second characteristic feature of these rules, that is to say their complexity. That applies not so much to the rules themselves as to their implementation and monitoring. It is not easy to ascertain whether and to what extent an undertaking charges real costs. That is because the rules generally involve supervision of the former monopoly-holders which not only have a dominant position on the market but often also, on account of that position, are the only ones with any insight into the economic soundness of the costs to be calculated. It goes without saying that they have an interest in ensuring that the costs calculated are not too low. The Commission's complaints relate to the costs which France Télécom may take into account. Do

they include only the costs of non-profitable telephone services, or also other costs? How are these costs calculated as real net costs?

16. The timetable within which liberalisation must be implemented forms a significant part of (the rules on) liberalisation. Its purpose is to overcome disparities in the level of liberalisation between the Member States which could result in distortion of competition between States.

17. I should also stress the social aim of the universal service. It is a public service, based on the view that the telephone is now an essential necessity of life. A Member State must be able to guarantee that the quality of this service, for which it is not itself responsible, is satisfactory.

18. In the light of those considerations it is not surprising that the Commission monitors closely the implementation of the Community rules by the Member States. Compliance with obligations in the telecommunications sector must be strict. I also take this as the main premiss of my Opinion. Having regard to the importance of strict compliance for the aim to be achieved, that is to say liberalisation of the telecommunications sector, and having regard to the fact that compliance in itself is difficult to monitor, I consider that the directive requires an interpretation centred on the wording of its provisions — that is to say a legalistic interpretation.

V — The complaints, the defence and the appraisal

19. The Commission has drawn up six complaints which I will reproduce in abridged form below. I will consider the defence in respect of each complaint and then make my appraisal.

The first complaint

20. The Commission contends that the requirement which France imposed on the operators of mobile telephone services — France Télécom's new competitors — to contribute to the universal service in respect of 1997 has no basis in Community law. That is because in 1997 France Télécom still enjoyed an almost complete monopoly over voice telephony. For that reason it should finance the universal service in full. Furthermore, the Commission considers that it is wrong to make providers of mobile telephone services contribute to the universal service on the fixed network.

21. In its defence, the French Government contends that the general nature of Article 4c of Directive 90/388, as amended by Directive 96/19, does not enable the operators of mobile telephone services to be excluded from financing the universal service. It does not consider that the French

system, which provided for a contribution from the operators of mobile telephone services as early as 1997, is inconsistent with the directive. What is more, any other interpretation of the directive would breach the principle of legal certainty. Article 4c requires that the net cost of the universal service be shared. Moreover, a mechanism for sharing the cost of the universal service prevents a single provider from having to bear the entire and disproportionate burden of the universal service.

22. The French Government argues that the central question is whether the introduction of mobile telephony affects the net cost of the universal service borne by France Télécom. That question has been answered — as early as 1997 — in the affirmative. It therefore considers that the contributions from the operators of mobile telephone services are an economic necessity.

23. In the view of the French Government, the directive does not establish an express link between the abolition of the monopoly over fixed telephony and the introduction of a financing mechanism for the universal service. The date on which the monopoly over voice telephony had to be abolished, 1 January 1998, has no bearing on the universal service.

24. In its reply, the Commission argues that the aim of maintaining the monopoly over fixed voice telephony until 1 January 1998 was precisely to allow the traditional provider to preserve its financial stability and provide a universal service. It refers *inter alia* to the fourth and twenty-sixth recitals in the preamble to Directive 96/19. As long as France Télécom had a monopoly over voice telephony, there was no need to make others contribute to the cost of the universal service. In that respect Article 5(1) of Directive 97/33 is clear: only '[w]here a Member State determines, in accordance with the provisions of this article, that universal service obligations represent an unfair burden on an organisation' can it establish a mechanism for sharing the net cost of the universal service obligations. In the view of the Commission, the file contains no indication that a national system for sharing the net cost was necessary or that the provision of universal service represented an unreasonable burden on France Télécom.

25. The Commission contends that the French Government's argument that the emergence of mobile telephony affects the cost of the universal service has no basis in fact. The emergence of mobile telephony has led to an increase in the traffic on France Télécom's network but has had no impact on the cost of the universal service.

26. In its rejoinder, the French Government examines the criterion relating to the need

for a system for cost sharing. Cost sharing may be necessary to abolish the monopoly over voice telephony. On the other hand, it does not necessarily have to follow such abolition. The French Government also refers, *inter alia*, to Article 86(2) EC.

27. In my appraisal I take it that the relevant provisions of Community law require universal service to be guaranteed only in respect of the public telephone network. The requirement does not apply to mobile telephony. Moreover, in France there is no universal service for mobile telephony.

28. In the light of this it is obvious that the cost of the universal service should be shared between the various providers of fixed telephony, the providers of mobile telecommunications not being required to contribute.

29. Naturally, the mobile telecommunications services have to use the fixed networks. Costs are charged for such use. These are the costs of interconnection which arise in accordance with Article 4 of Directive 97/33. In my view, a distinction must be drawn between such costs and the cost of the universal service to which the Commission's complaints relate. The fact that Article 5(2) of Directive 97/33 provides that '[c]ontributions to the cost of universal service obligations if any... may take the form of a supplementary charge added to the interconnection charge' changes nothing in that respect.

30. Furthermore, as the Commission argues and the French Government does not deny, in 1997 France Télécom enjoyed an almost total monopoly over voice telephony. Therefore, there was no 'unfair burden' as referred to in Article 5(1) of Directive 97/33 if France Télécom had to bear the full cost of the universal service obligations. Moreover, it is not possible to draw any other conclusion from Article 4c(a) and (b) of Directive 90/388, as amended by Directive 96/19, which merely lays down the conditions to be satisfied by the national scheme necessary for sharing the cost of the universal service. I consider that the scheme for sharing the net cost in this case is not one which is necessary under Article 4c.

31. I need not point out that the French Government was quite unable to show that the emergence of mobile telephony has led to an increase in the net cost of the universal service. Finally, the French Government also refers to the (possible) relationship between abolishing the monopoly over fixed voice telephony and sharing the cost of the universal service. Although I

certainly agree with the French Government that the universal service and the abolition of the monopoly are obligations which must be distinguished and fulfilled separately from one another, I consider that that is not relevant to the appraisal of this complaint of the Commission.

32. I therefore conclude that the Commission's first complaint is well founded.

The second complaint

33. The Commission points out that Article 4c of Directive 90/388, as amended by Directive 96/19, requires the Member States to allow their telecommunications providers 'to re-balance tariffs'. The aim is to correct imbalances in tariffs whereby certain tariffs, such as subscriptions for households and tariffs for local calls, were kept artificially low, and other tariffs, such as long-distance and international calls, were kept artificially high. The imbalance in tariffs has an unfavourable effect on competition. Fixing low tariffs for certain segments makes it more difficult for newcomers to the market to compete. They are thus discouraged from making investments. Article R 35-3(II) of the Code provided for the balancing of tariffs by 31 December 2000. However, the directive requires that where such rebalancing cannot be completed before 1 January 1998 the Member State concerned must report to the Commission on the plans for phasing out the remaining tariff imbalances. This must include a detailed timetable for implementation.

34. The Commission states that no timetable was submitted to it even though this should have occurred before 11 January 1997. Consequently, it was unable to determine whether or not France had fulfilled its obligations under Article 4c of Directive 90/388, as amended by Directive 96/19, read in conjunction with the first paragraph of Article 2 of Directive 96/19.

35. In that respect the Commission adds the following comments. Assuming that the tariff of FRF 65, excluding tax, given in a ministerial decree of 29 September 1999 as the balancing tariff for telephone subscriptions was also *de facto* the balancing tariff, the new France Télécom subscription tariff of FRF 64.48, excluding tax, in force since 1 March 1999 was too low. The balancing required by the directive had not yet been completed. In the view of the Commission, the French authorities had indicated that as from 1 March 1999 the cost of the imbalance until the end of the year was still FRF 16 million. This cost had to be financed by the universal service fund. The Commission

considers that the French authorities should thus concede that the balancing had not yet been completed in accordance with their own criteria. The French authorities should either have confirmed that France Télécom was authorised to continue raising its tariffs or have notified the timetable provided for in Article 4c of Directive 90/388, as amended by Directive 96/19.

36. In its defence, the French Government states that it disagrees with the Commission as regards the content of the obligation to re-balance tariffs.

37. It argues that competition between telecommunications providers takes place primarily on the market in long-distance and international calls. This led the traditional provider to pay for the cost of connection to the local loop from subscriptions and revenue from local calls. The French Government considers that this was acceptable. As a result, the cost of the local segment was no longer subsidised from the proceeds from long-distance calls. Furthermore, in September 1999 a subscription tariff was set which was almost identical to the balancing tariff of FRF 65. In that regard account was taken of France Télécom's financial data.

38. As regards the timetable, the French Government observes that the directive lays down only final dates, not mandatory intermediate stages. Balance, as the French Government perceives it, was achieved in France well before 31 December 2000. The absence of balance could, according to the wording of Directive 90/388, as amended by Directive 96/19, have the effect of increasing the net cost of the universal service. A mechanism for sharing these costs could temporarily take the place of the balance in tariffs. The French Government also draws a distinction between a deficit resulting from local access — which France Télécom makes up through revenue from local calls — and other very minor deficits.

39. In its reply, the Commission contends that the directive requires balancing on the basis of real costs, whereas the French Government in its analysis mixes up all kinds of costs and revenues. The costs of each individual element must be compared with the price which is charged for it. The French approach is unfavourable to competition and makes it almost impossible for newcomers to enter the market. The figures which the French Government produces reveal a deficit. The revenues were considerably lower than the costs.

40. In its rejoinder, the French Government acknowledges that the proceeds from telephone subscriptions were not sufficient to

cover all connection costs. The deficit was made up through the tariffs which France Télécom charges for local calls. As a result there was still no balance, on the definition applied by the Commission. The French Government explains that competition for local calls would be possible only as of 1 January 2001, following the unbundling of the local loop. It also points out that it was very difficult to work to a timetable with intermediate stages. Fixing a realistic final date was consistent with the objectives of the directive and was also transparent for newcomers to the market.

41. In assessing the second complaint, it is important first to establish which requirements Article 4c of Directive 90/388, as amended by Directive 96/19, lays down as regards the balancing tariff to be achieved. The Commission and the French Government disagree in this respect. I will rely primarily on the 20th consideration in the recital to the directive. As regards the cost structure, it identifies five different types of costs: initial connection, the monthly rental, local calls, regional calls and long-distance calls. In my view, the wording of Article 4c of the directive is unequivocal. A tariff must be achieved on the basis of real costs in respect of all five types of costs. This means that the subscription tariff (the monthly rental) must also correspond to the real costs.

42. The requirement relating to a cost structure based on real costs must be viewed in the light of the underlying purpose of the Community legislation, that is to say the liberalisation of the telecommunications market. The calculation of an excessively low tariff could give France Télécom, the former monopoly-holder, an unfair advantage, because competitors would have to charge even lower tariffs to induce potential customers to switch their subscriptions from France Télécom to them. It should be obvious that excessively low tariffs can deter possible competitors from entering the market. For these reasons I consider that undercutting of the balancing tariff is unjustified.

43. Since the parties agree that the tariff of FRF 64.68 applied by France Télécom differed — albeit slightly — from the real costs, the balance sought by the directive was not achieved. It is of no relevance — assuming that the claim by France Télécom is factually correct — that the deficit in respect of the subscription tariffs collected was covered by the tariffs for local calls and that the effect on competition of this imbalance was minimal, or even non-existent.

44. This means that, in accordance with the abovementioned Article 4c, the French Government should have reported to the Commission on how it intended to phase out the imbalance. The directive requires such a report to include a detailed time-

table. In my view, it is established that the requirement relating to a detailed timetable cannot be satisfied merely by stating a final date. Nor am I able to concur with the French Government's contention that no mandatory intermediate stages are required.

45. In the light of the foregoing, I conclude that the second complaint is also well founded.

The third complaint

46. The Commission contends that the method of calculating the net cost of the universal service does not satisfy the requirements of the directive. Firstly, the profitable household subscriptions were wrongly included. Secondly, the calculation was not carried out in a transparent and objective manner.

47. The Commission maintains, in the first part of the complaint, that the French legislation was inconsistent with Article 5(3) of Regulation 97/33, read in conjunction with Annex III thereto, since the calculation formula in Article R 20-32 of the Code included the costs of profitable customers. In the view of the Commission, a customer is profitable where the revenues he furnishes to the telecommunications provider are greater than the costs which the provider incurs in serving him. The directive requires that a Member State determine selectively which customers are to contribute to the net cost of the universal service. Component C1 of the French Law was not selective.

48. In the second part of the complaint the Commission argues that the calculation formula in component C1 contains no objective criteria for allocating the burdens associated with the financing of the universal service to the various telephone providers, contrary to Article 4c of Directive 90/388, as amended by Directive 96/19. Furthermore, the principle of transparency laid down in Article 5(1) of Directive 97/33 was not observed.

49. The calculation formula had two specific flaws. Firstly, the Commission objects to the reference value Pe. This reference value affected the amount deducted from components C1 and C2 and thus the contributions from the various telecommunications providers. It should therefore have been fixed in a transparent manner. There is no indication in the figures which the French Government provided in response to the reasoned opinion that it was.

50. Secondly, the reference values P and Pe are not comparable. A key element in determining the cost of the universal service is the difference between the real price of the telephone subscription (P) and the 'balanced' price (Pe) which is based on practices in other countries. A comparable basis for the reference values is necessary in order to be able to calculate that difference. There is no such basis in the present case.

51. In the view of the Commission, the first difference between the reference values P and Pe is as follows. In the countries of reference the detailed billing of customers forms part of the basic subscription, whereas this type of billing is optional for customers of France Télécom. This difference results in an artificial increase in the value Pe, adding (in 1998) FRF 351 million to the costs of component C1. The second difference is that the value Pe included costs incurred in maintaining the so-called 'red list', whereas the value P did not relate to the revenue which flowed therefrom. The red list is made up of subscribers who do not wish to be listed in the telephone directory.

52. In the defence, the French Government refers — in response to the first part of the third complaint — to point (i) in the fourth paragraph of Annex III to Directive 97/33, which provides, in so far as it is relevant, that it is possible to include specific end-users or groups of end-users who can only be provided with the specified network and services at a loss or under cost conditions falling outside normal commercial standards. The directive does not refer to the distinction between profitable and non-profitable costs. The French Government concludes that it follows from the word 'or' in the abovementioned clause that costs other than those which can be incurred 'only... at a loss' (that is to say non-profitable costs) may be included. Furthermore, the wording of the annex shows that the list of elements which may be taken into account in calculating the cost of the universal service is not exhaustive.

53. The second part of the third complaint leads the French Government to argue as follows. The price of FRF 65 for the subscription stemmed from a comparison between the countries in which the tariff has been balanced. This price falls within the margin of between FRF 55 and FRF 75 defined in the Champsaur report. Furthermore, the decision of the ART of 9 January 1999 (No 99-120) increasing the subscription tariff to FRF 64.68 achieved a balance in practice. In short, the value Pe is sufficiently transparent.

54. In its reply, the Commission contends that the French Government has not put

forward a single argument to explain the fact that all subscribers in France are regarded as subscribers who are served 'under cost conditions falling outside normal commercial standards'. Moreover, the Commission considers that the French Government has failed to give a proper explanation of the basis for the flat-rate amount of FRF 65 for the value Pe. The margin indicated by the Champsaur report is very broad. Furthermore, the report itself states that a more precise calculation is necessary.

55. In its rejoinder, the French Government again points out that it was not possible — before the balancing of tariffs was achieved — to identify the subscribers served in accordance with normal commercial standards.

56. I take the following view as regards the first part of the complaint. Annex III to Directive 97/33 lays down rules for the calculation of the net cost of universal service provision. It provides a limited and as precise as possible a description of the costs which may be included. In my view, the description shows quite clearly that only costs which result directly from universal service provision may be included. The provider under the obligation to provide the universal service must not be burdened disproportionately by that obligation but, by the same token, may not derive any financial benefit from it. This is consistent with the context of the system, which is intended precisely to create equal market conditions for the various telecommunications providers. The creation of such a fair market requires a clear cost structure in which the costs of a certain type of activity are not increased in order to be able to provide other services more cheaply.

57. Costs may be included where they are attributable to activities which may only be engaged in at a loss or under cost conditions falling outside normal commercial standards. These are, in so far as I understand the annex, activities which a commercial operator would not carry out unless he were subject to the universal service obligation. Consequently, I consider that the Commission is also right to maintain that the costs must relate to non-profitable activities. They do not necessarily have to relate to loss-making activities but may also relate to the costs of activities which, viewed in terms of normal economic management, provide insufficient returns. By way of example, the annex refers *inter alia* to the installation and operation of public telephone boxes. That need not be a loss-making activity. It may be that the risk is so great that a company would, after undertaking a normal commercial assessment, decide not to instal them. I do not agree with the French Government that the directive draws no distinction between profitable and non-

profitable costs. I consider that non-profitable is a broader term than loss-making.

58. I take the view that the Commission has demonstrated adequately that the French legislation does not comply with the criteria laid down in Annex III to the directive. The calculation effected on the basis of Article R 20-32 of the Code did not sufficiently limit the costs to be included, since the costs of all telephone subscriptions in France were included. In that connection I should repeat that the annex to the directive refers precisely to the costs which may be attributed to specific end-users or groups of end-users. Finally, in its rejoinder the French Government still contends that it was not possible to identify subscribers who are served in accordance with normal commercial standards. Irrespective of whether or not that view is correct, even in such a case Annex III to Directive 97/33 must be interpreted strictly and the French Government should have endeavoured to comply with the annex by other means.

59. The second part of the third complaint, which relates to the appropriateness of the reference value Pe, leads me to make the following remarks. In general, I consider that bench-marking is an appropriate method of establishing a criterion for calculating the net cost of the universal service. In the light of the differences between the Member States, the result of such bench-marking must be used prudently. That is certainly the case where specific activities are optional in certain countries of reference but not in the Member State with which the comparison is being drawn. I consider that the French Government's argument that the differences noted by the Commission were not relevant to the application of the reference value Pe is not sufficient. Furthermore, I agree with the Commission that the margin which the Champsaur report applies on the basis of bench-marking is very broad.

60. In the light of the foregoing, I conclude that that method of calculating the net cost does not comply with Article 5(3) of the directive, read in conjunction with Annex III thereto. Therefore, the third complaint is also well-founded.

The fourth complaint

61. The Commission contends that certain components of the cost of the universal service were fixed on a flat-rate basis, contrary to the specific method of calculation laid down in Article 5(3) of Directive 97/33. This complaint breaks down into three parts.

62. In the first part the Commission contends that Article R 20-33(III) of the Code fixed the net cost relating to non-profitable subscribers in profitable zones at an arbitrary level of 1% of turnover. This percentage was higher than the estimates made in other countries. In the defence, the French Government argues as follows. The Champsaur report shows that in 1997 there was still no reliable method for calculating such costs. The report settled on a margin on which the level of 1% was based. The French Government doubts whether it is possible to calculate the costs relating to 1997 retrospectively. In any event, the ART does not have the relevant data. In its reply, the Commission does not accept the French Government's explanation. In support of its position, it submits a table showing that the flat-rate amounts relating to 1997 and 1998 are much higher than the amounts relating to 1999 and 2000, when the calculation was made on the basis of a model. In its rejoinder, the French Government stresses that the method applied in 1997 and 1998 was the only reliable method even though it was, of necessity, imprecise. Moreover, the method applied had little significance in respect of competing telecommunications providers since their position in 1997 and 1998 was still a minor one.

63. The second part of the Commission's complaint concerns Article 3 of the decree, which fixed the net cost of the universal service in respect of 1997 at a flat rate. According to the French Government, the calculation of the geographical component at 3% of turnover stemmed from an international comparison. The French Government points out that it had opted for a pragmatic approach. A complex calculation thereafter — in respect of 1997 — would result in only a very marginal alteration to the contributions from the providers. In its reply, the Commission notes that the French Government explains which elements were involved but not how it had arrived at an amount on the basis of those elements. This the French Government denies in its rejoinder. It considers that it is technically possible to apply the methodology followed in 1999 to 1997 and 1998 but that it is difficult to do so. France Télécom would have to provide a great deal of information for the sake of a marginal result. Furthermore, opening up the possibility of subsequently choosing another methodology would lead to uncertainty on the part of traders.

64. The third part of the complaint relates to the hardship tariffs. In the view of the Commission, the contributions paid to France Télécom to offset the costs of certain hardship tariffs were calculated in an imprecise manner. In the defence, the French Government refers to the decree of 8 March 1999 (No 99-162) amending Articles R 20-34 and R 20-40 of the Code and Article R 251-28 of the Code de la sécurité sociale in which a new system was introduced. This system included a reduction for minimum wage earners and disabled war veterans of FRF 27.60 a month (in 2000). The reduction was paid for from

a universal service fund to which the telephone providers had to make a contribution proportionate to their turnover. Moreover, in special cases the State was able to assume specific telephone debts at the request of those concerned. A financial ceiling of 0.8% of telephony-related turnover applied to the entire system. The Commission responded in the reply as follows: the infringement in respect of 1997 and 1998 remained, irrespective of the recently introduced system relating to hardship tariffs.

65. The Commission's fourth complaint relates essentially to the extent to which Article 5(3) of Directive 97/33, read in conjunction with Annex III thereto, permits a flat-rate calculation of the net cost. As I have already stated in my appraisal of the third complaint, the directive requires a precise calculation of the net cost. It states specifically how the costs are to be calculated. In my view, the directive does not permit a flat-rate calculation. Therefore, I also consider that the fourth complaint is well founded in so far as it relates to the method of calculation applied in France in 1997 and 1998. A different method of calculation has been used since 1999. That is not covered by the present dispute.

The fifth complaint

66. The Commission's fifth complaint relates to certain other components of the cost of the universal service which were drawn up in such a way that they resulted in an artificial increase in costs.

67. It relates firstly to the incorrect calculation of the net cost of non-profitable zones. The method applied failed to include certain proceeds such as those stemming from inclusion in the red list, which consists of subscribers who do not wish to be listed in the telephone directory, and from so-called 'comfort services'. In this respect the Commission considers that it is significant that France Télécom has provided no data. In the defence, the French Government concedes that the costs of and proceeds from the 'comfort services' have been taken into account only since 1999. It disputes the Commission's contention in so far as it concerns inclusion in the red list. According to the French Government, the maintenance of the red list cannot be separated from the publication of an annual telephone directory. Therefore, the red list does not form a separate cost component.

68. In its reply, the Commission notes that the French Government's acknowledgement that it acted incorrectly as regards the proceeds from 'comfort services' until 1999 is not accompanied by any resolve to remedy the situation. It therefore maintains this part of the complaint. The Commission goes on to observe that the administration of the red list and the publication of a paper

or electronic telephone directory are separate activities. In that respect it refers to Article 6(2) and (3) of Directive 98/10. Those provisions require every provider to keep a red list for its own subscribers. The costs thereof are separate from the costs of and proceeds from the telephone directory. In its rejoinder, the French Government maintains its view.

69. Secondly, the Commission complains that in respect of 1998 the French authorities included traditional data in the calculation and did not apply best practice. It refers to Annex III to Directive 97/33, which provides that costs and revenues should be forward-looking. In the defence, the French Government contends that as far as was possible account was taken of the Commission's recommendations relating to the application of Annex III to Directive 97/33. In its reply, the Commission contends that France acknowledges that it failed to fulfil its obligations in respect of 1998. In its rejoinder, the French Government refers to the difficulties in terms of application which would arise if the correct methodology, which was applied in 1999, had had to be applied to 1998.

70. Thirdly, the Commission contends that, with the exception of the proceeds from public pay telephones and the provision of telephone directories, no account was taken of the intangible benefit accruing to France Télécom as a result of providing the universal service. Article 5(4) of Directive 97/33 requires that account be taken of the market benefit if any which accrues to the provider which offers the public service. The Commission gives certain examples of benefits which may accrue to France Télécom and which could have been taken into account. In the defence, the French Government concedes that Article 5(4) was not complied with. It adds that it is not possible to estimate the cost of the universal service retrospectively.

71. In appraising this complaint it is important to note that on almost all counts the French Government concedes that it failed to comply with the directive. In my view, that acknowledgment makes the complaint well founded. On one count, which relates to the red list, the French Government does not agree with the Commission. However, on that count, too, I conclude that the complaint is well founded. To me it is clear that the maintenance of the red list is a separate activity from the publication of a telephone directory. The cost of maintaining this list can also be regarded as a separate cost component. In that respect the following considerations apply. The red list is maintained with a view to managing subscriptions and has, in itself, nothing to do with the universal service. On the other hand, the publication of a telephone directory forms — under Directive 98/10 — part of the universal service. For those reasons, the subscribers of all other providers should — in a competitive environment — also be included in the telephone directory, with the costs and proceeds which that entails.

The sixth complaint

72. The Commission considers that France has failed to comply fully with the second subparagraph of Article 5(5) of Directive 97/33. The report which the French authorities drew up in respect of 1997 omits to show what contributions the parties concerned made to the net cost of the universal service. The French Government acknowledges that the reports in respect of 1997 and 1998 do not comply fully with the requirements of Directive 97/33.

73. Since the French Government acknowledges that the reports which it drew up in respect of 1997 and 1998 do not comply with the requirements of Article 5(5) of Directive 97/33, I conclude that the sixth complaint is well founded.

VI — Conclusion

74. In the light of the facts and circumstances set out above, I propose that the Court should:

(a) declare that by failing to adopt the laws or regulations necessary to implement Article 4c of Commission Directive 90/388/EEC of 28 June 1990 on competition in the markets for telecommunications services, as amended by Directive 96/19/EC, and to implement Articles 5(1), (3), (4) and (5) of

Directive 97/33/EC of the European Parliament and of the Council of 30 June 1997 on interconnection in Telecommunications,

or, in any event, by failing to inform the Commission of such laws or regulations,

the French Republic has failed to fulfil its obligations under the above-mentioned directives.

(b) order the French Republic to pay the costs pursuant to Article 69(2) of the Rules of Procedure.