JUDGMENT OF THE COURT (Fifth Chamber)

7 January 2004 *

In Case C-500/01,

Commission of the European Communities, represented by S. Rating, acting as Agent, with an address for service in Luxembourg,

applicant,

v

Kingdom of Spain, represented by S. Ortiz Vaamonde, acting as Agent, with an address for service in Luxembourg,

defendant,

* Language of the case: Spanish.

APPLICATION for a declaration that, by failing to adopt the laws, regulations and administrative provisions necessary to comply with Article 4(c) of Commission Directive 90/388/EEC of 28 June 1990 on competition in the markets for telecommunications services (OJ 1990 L 192, p. 10) as amended by Commission Directive 96/19/EC of 13 March 1996 (OJ 1996 L 74, p. 13), the Kingdom of Spain has failed to fulfil its obligations under those directives and the EC Treaty,

THE COURT (Fifth Chamber),

composed of: P. Jann, acting for the President of the Fifth Chamber, D.A.O. Edward (Rapporteur) and A. La Pergola, Judges,

Advocate General: P. Léger,
Registrar: R. Grass,

having regard to the report of the Judge-Rapporteur,

after hearing the Opinion of the Advocate General at the sitting on 10 July 2003,

gives the following

Judgment

1 By application lodged at the Court Registry on 21 December 2001, the Commission of the European Communities brought an action under Article 226 EC for a declaration that, by failing to adopt the laws, regulations and administrative provisions necessary to comply with Article 4(c) of Commission Directive 90/388/EEC of 28 June 1990 on competition in the markets for telecommunications services (OJ 1990 L 192, p. 10) as amended by Commission Directive 96/19/EC of 13 March 1996 (OJ 1996 L 74, p. 13) ('Directive 90/388'), the Kingdom of Spain has failed to fulfil its obligations under those directives and the EC Treaty.

Legal background

Community legislation

2 The fifth recital in the preamble to Directive 96/19 states:

'... In order to allow telecommunications organisations to complete their preparation for competition and in particular to pursue the necessary rebalancing of tariffs, Member States may continue the current special and exclusive rights

regarding the provision of voice telephony until 1 January 1998. Member States with less developed networks or with very small networks must be eligible for a temporary exception where this is warranted by the need to carry out structural adjustments and strictly only to the extent necessary for those adjustments. Such Member States should be granted, upon request, an additional transitional period respectively of up to five and of up to two years, provided it is necessary to complete the necessary structural adjustments. The Member States which may request such an exception are Spain, Ireland, Greece and Portugal with regard to less developed networks and Luxembourg with regard to very small networks...'

3 According to the 20th recital in the preamble to Directive 96/19:

'... Member States should phase out as rapidly as possible all unjustified restrictions on tariff rebalancing by the telecommunications organisations and in particular those preventing the adaptation of rates which are not in line with costs and increase the burden of universal service provision.'

4 Article 4(c) of Directive 90/388, introduced by Article 1(6) of Directive 96/19 provides:

'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 rebalance 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.

In any case, within three months after the European Parliament and the Council adopt a Directive harmonising interconnection conditions, the Commission will assess whether further initiatives are necessary to ensure the consistency of both Directives and take the appropriate measures.

In addition, the Commission shall, no later than 1 January 2003, review the situation in the Member States and assess in particular whether the financing schemes in place do not limit access to the relevant markets. In this case, the Commission will examine whether there are other methods and make any appropriate proposals.'

5 On 10 June 1997, the Commission adopted Commission Decision 97/603/EC concerning the granting of additional implementation periods to Spain for the implementation of Directive 90/388/EEC as regards full competition in the telecommunications markets (OJ 1997 L 243, p. 48). Article 1 of that decision authorises the Kingdom of Spain to postpone until 1 December 1998 the effective granting of further licences for the provision of voice telephony and public telecommunications networks.

6 Regulation (EC) No 2887/2000 of the European Parliament and of the Council of 18 December 2000 on unbundled access to the local loop (OJ 2000 L 336, p. 4) should, according to its second recital, complement the existing provisions of Community law guaranteeing universal service and affordable access for all citizens of the European Union by enhancing competition, ensuring economic efficiency and bringing maximum benefit to users.

7 According to the seventh recital in the preamble to that regulation, unbundled access to the local loop allows new entrants to compete with notified operators in offering high bit-rate data transmission services for continuous internet access and for multimedia applications based on digital subscriber line (DSL) technology as well as voice telephony services.

8 Article 3(3) of Regulation No 2887/2000 provides:

'... notified operators shall charge prices for unbundled access to the local loop and related facilities set on the basis of cost-orientation.'

National legislation

9 The Spanish authorities adopted the Orden por la que se determinan las tarifas y condiciones de interconexión a la red adscrita al servicio público de telefonía básica que explota el operador dominante para la prestación del servicio final de telefonía básica y el servicio portador soporte del mismo (Order fixing tariffs and interconnection conditions to the public network of voice telephony exploited by the dominant operator) of 18 March 1997 (BOE No 74 of 27 March 1997, p. 10079). That measure increased the price of the monthly subscription charge by 16% and the price of local calls by 13%, and reduced the price of provincial calls by 5%, interprovincial calls by 15% and international calls by 12%.

10 The Orden sobre reequilibrio tarifario de servicios prestados por 'Telefónica Sociedad Anónima' (Order rebalancing the tariffs of services offered by Telefónica SA) of 31 July 1998 (BOE No 188, of 7 August 1998, p. 26858), set the monthly telephone line rental charge at ESP 1 442 for 'residential lines' and ESP 1 797 for 'trunk lines'.

11 Real Decreto-Ley 16/1999 por el que se adoptan medidas para combatir la inflación y facilitar un mayor grado de competencia en las telecomunicaciones

(Royal Decree-Law adopting measures to counter inflation and increase competition on the telecommunications market) of 15 October 1999 (BOE No 248 of 16 October 1999, p. 36561) provided for new increases of telephone subscription charges. According to the timetable envisaged, the charge had to increase ESP 100 three times: on 1 August 2000, 1 March 2001 and 1 August 2001.

12 By the Orden por la que se dispone la publicación del Acuerdo de la Comisión Delegada del Gobierno para Asuntos Económicos de 27 julio de 2000, por el que se establece un nuevo marco regulatorio de precios para los servicios prestados por 'Telefónica de España, Sociedad Anónima Unipersonal' (Order for the publication of the agreement of the Government Representative for Economic Affairs of 27 July 2000 establishing a new price mechanism for the services offered by Telefónica SA) of 31 July 2000 (BOE No 183, of 1 August 2000, p. 27564) a new 'price cap' pricing system, based on a capping mechanism, was introduced for the period 2001-2002. It is based on calculation formulae involving Spanish Government forecasts of changes in the retail price index ('RPI') and adjustment factors.

13 The price cap system was maintained in force for 2003 by the Orden por la que se dispone la publicación del Acuerdo de la Comisión Delegada del Gobierno para Asuntos Económicos del Acuerdo por el que se modifica el Acuerdo de 27 de julio de 2000, por el que se establece un nuevo marco regulatorio de precios para los servicios prestados por 'Telefónica de España, Sociedad Anónima Unipersonal') (Order for the publication of the decision of the Government Commission on Economic Affairs amending the decision of that commission of 27 July 2000 establishing a new pricing mechanism for the services offered by Telefónica SA) of 10 May 2001 (BOE No 118, of 17 May 2001, p. 17456). Under that pricing system:

— all fixed telephony and fixed calls to mobile telephony shall be subject to a regulated charge equivalent to the annual variation in the forecast RPI - 9%

in 2001, the annual variation in the forecast RPI - 8% in 2002 and to the annual variation in the forecast RPI - 4% in 2003;

— the subscription charges may not rise in 2001, but may be increased by a maximum of the annual variation in the forecast RPI + 9.4% in 2002 and by the annual variation in the forecast RPI + 6% in 2003;

— connection charges may rise by a maximum of the annual variation in the forecast RPI - 16.5% in 2001 and 2002 and by the annual variation in the forecast RPI - 2% in 2003.

14 Real Decreto-Ley 7/2000 de Medidas Urgentes en el Sector de las Telecomunicaciones (Royal Decree-Law on urgent measures in the telecommunications sector) of 23 June 2000 (BOE No 151, of 24 June 2000, p. 22458) imposed a duty to provide full unbundled access and shared access to the local loop. That measure was supplemented by Real Decreto 3456/2000 por el que se aprueba el Reglamento que establece las condiciones para el acceso al bucle de abonado de la red pública telefónica fija de los operadores dominantes (Royal Decree approving the rules establishing the terms of access to the loop for subscribers to the fixed public telephony network of the dominant operators) of 22 December 2000 (BOE No 307, of 23 December 2000, p. 45567). Article 5(1) of the latter royal decree provides that the rates for access to the local loop must be set on the basis of cost orientation.

15 The Orden por la que se dispone la publicación del Acuerdo de la Comisión Delegada del Gobierno para Asuntos Económicos, por el que se establecen los precios de la primera oferta de acceso al bucle de abonado en las modalidades de

acceso completamente desagregado, de acceso compartido y de acceso indirecto, a la red pública telefónica fija de 'Telefónica de España, Sociedad Anónima Unipersonal' (Order for the publication of the agreement of the Government Representative for Economic Affairs setting the prices of first offering of access by subscribers to the loop and the full unbundled access, shared access and indirect access to the Telefónica fixed public telephony network) of 29 December 2000 (BOE No 131, of 30 December 2000, p. 49758), sets the monthly rates for unbundled access to the local loop. Those are ESP 2 163 in 2001, ESP 2 100 in 2002 and ESP 2 050 in 2003.

Pre-litigation procedure

16 The pre-litigation procedure consisted of two successive stages.

17 In the first stage the Commission sent a letter of formal notice to the Kingdom of Spain on 11 December 1998 reminding it that it had not yet notified the Commission of a detailed timetable for the phasing out of restrictions on tariff rebalancing in accordance with Article 4(c) of Directive 90/388.

18 On 11 February 1998 the Spanish authorities replied that the Orden of 31 July effected the tariff rebalancing and that the timetable could be spread over the period to 31 December 2000.

19 Taking the view that the measures adopted by the Spanish authorities were inadequate, and that the latter acknowledged that they had not drawn up a detailed timetable for the implementation of those measures, the Commission issued a reasoned opinion on 4 May 1999.

20 By letter of 26 April 1999, the Spanish authorities notified the Commission of the new measures for the reduction of the provincial, interprovincial and international call rates.

21 In order to take account of those measures the Commission informed the Kingdom of Spain, by letter of 26 May 1999, that the reasoned opinion of 4 May 1999 had been superseded.

22 In the second stage of the pre-litigation procedure the Commission continued its inquiry into the case in the light of a complaint lodged on 23 November 1998 by the traditional operator Telefónica de España SA ('Telefónica'). On 25 November 1999 the Commission requested certain information from the Spanish Government concerning that complaint. By letter of 21 January 2000 the Spanish authorities replied that it was impossible for them to ascertain the existence of the access deficit alleged by Telefónica. Moreover, they informed the Commission of their intention to implement the price cap system.

23 On 4 May 2000, the Commission sent a new letter of formal notice to the Kingdom of Spain. It complained that Spain had not allowed Telefónica sufficient flexibility to enable it to effect the tariff rebalancing required under Article 4(c) of Directive 90/388.

24 Since it was not satisfied by the reply given by the Spanish authorities to that letter, the Commission issued a new reasoned opinion on 29 January 2001. In that opinion it pointed out that the process of tariff rebalancing had not been completed in 1999 and that it would also probably not be completed in 2001

either. The Commission further stated that Telefónica's access deficit in 1999 was ESP 258 billion, and it called on the Kingdom of Spain to take the measures necessary to comply with the reasoned opinion within a period of two months from its notification.

25 In their reply of 29 March 2001, the Spanish authorities disputed the Commission's assessment. They submitted that Telefónica's alleged access deficit in 1999 was ESP 173 449 billion, ESP 85 million less than the figure put forward by the Commission. Moreover, the Spanish authorities announced a series of amendments to the price cap system.

26 On 18 April 2001 Telefónica stated that as a result of the measures announced by the Spanish Government it was withdrawing its complaint.

27 On 27 July 2001, the Commission sent a supplementary reasoned opinion to the Kingdom of Spain to take account of the adoption of certain provisions requiring Telefónica to offer unbundled access to the local loop, amendments to the price cap system adopted in May 2001 and the exact assessment by the Spanish Government of Telefónica's access deficit for 1999.

28 The Spanish authorities replied to the supplementary reasoned opinion by letter of 9 October 2001. Not satisfied with that reply, the Commission brought the present action.

The infringement

Arguments of the parties

29 The Commission complains that the Kingdom of Spain has not applied correctly the Community rules on tariff rebalancing. It argues that the Spanish authorities should have authorised Telefónica to rebalance its tariffs as laid down by Directive 90/388. By requiring Telefónica to maintain a tariff structure which harmed its competitors, distorting their financial calculations and maintaining over a long period tariffs which were inconsistent with the underlying costs, the Spanish authorities created a situation detrimental to the development of competition, specifically in the context of unbundled access to the local loop.

30 The Commission argues that by taking account of the constraints imposed by the price cap system, the monthly subscription charges cannot be based on the real costs before the beginning of 2003. In that regard, it points out that the productivity gains of 6% per year claimed by the Spanish authorities, to eliminate the access deficit, are improbable, inasmuch as the infrastructure efficiency gains are modest.

31 The Spanish Government submits that Article 4(c) of Directive 90/388 does not mean that it must impose on Telefónica tariffs based on real costs: neither does it impose a precise period in which to fulfil the obligation to phase out restraints to tariff rebalancing. That provision merely requires it to phase out the restraints

preventing Telefónica from aligning its tariffs with real costs. In the absence of a period prescribed in Article 4(c), the question whether a Member State has failed to fulfil its obligations must therefore be assessed according to the circumstances prevailing in the Member State at the end of the period laid down by the reasoned opinion of 29 January 2001. Since Telefónica did not report any deficit in 2002 and 2003 which is, moreover, borne out by the fact that it has withdrawn its complaint, the Spanish authorities cannot be criticised for any failure to fulfil obligations.

Findings of the Court

32 Although Article 4(c) of Directive 90/388 does not lay down a period within which the obligation to rebalance tariffs must be fulfilled, the fact remains that several elements of Directive 96/19 state that the rebalancing of tariffs must be carried out at a sustained rate in order to facilitate the opening of the telecommunications market to competition. Thus, as the Advocate General stated in paragraphs 58 to 60 of his Opinion, it is clear from reading the 20th and 5th recitals in the preamble to Directive 96/19 together with Article 4(c) of Directive 90/388 that the Member States were bound to phase out the restrictions on tariff rebalancing as soon as possible after the entry into force of Directive 96/19 and at the latest by 1 January 1998. The Member States with less developed networks or with very small networks were to adopt a detailed timetable for the implementation of their obligation.

33 However, the Spanish Government has not shown that it had adopted, in accordance with Article 4(c) of Directive 90/388, such a timetable within the prescribed period and that it had been approved by the Commission.

34 As for Decision 97/603, it does not authorise the Kingdom of Spain to postpone the implementation of its obligation to phase out the restrictions on tariff rebalancing before 1 January 1998. It only permits the Kingdom of Spain to postpone until 1 December 1998 the effective grant of new licences for the supply

of vocal telephony and public telecommunications networks, the notification to the Commission, the publication of all the licensing and declaration procedures for the provision of voice telephony and the establishment of public telecommunications networks, and of the details of the national scheme envisaged to share the net cost of the provision of the universal service obligation.

35 In its defence, the Spanish Government expressly acknowledged that Telefónica had experienced an access deficit of ESP 173 449 billion in 1999, and that that access deficit was absorbed, according to the most optimistic estimates of the annual gains in productivity, only during 2002. It also acknowledged the existence of a difference between the monthly subscription charge and the charge for access to the local loop.

36 As regards the question whether the Spanish authorities can be held responsible for the deficit, it must be recalled that until the entry into force of the price cap system in 2001 they themselves carried out the various increases and reductions in the charges for the components of the voice telephony services, so that the traditional operator had no discretion in setting the charges. As the Advocate General stated in paragraphs 88 and 89 of his Opinion, the absence of tariff rebalancing for 1999 and 2000 is exclusively attributable to the Spanish authorities.

37 It is true that after the introduction of the price cap system in 2001 Telefónica was authorised to increase or reduce its prices each year. However, the tariff imbalances recorded for 2001 and 2002 cannot be entirely attributed to it; a part of those tariff imbalances must be attributed to the Spanish authorities. Telefónica's freedom to set charges was limited by the existence of a ceiling or

maximum price imposed by the Spanish authorities. That restriction was detrimental to the development of competition with regard to the traditional operator and is contrary to the aim of Directive 90/388.

38 Since the tariff rebalancing required by Article 4(c) of Directive 90/388 can be carried out by the traditional Spanish operator only for the beginning of 2003, that is with a five year delay with respect to the requirement of Directive 90/388, both the tariff imbalance and the situation detrimental to the development of competition arising from it are attributable to the Spanish authorities.

39 It must therefore be held that by failing to adopt the laws, regulations and administrative provisions necessary to comply with Article 4(c) of Directive 90/388, the Kingdom of Spain has failed to fulfil its obligations under that directive.

Costs

40 Under Article 69(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. Since the Commission has applied for costs and the Kingdom of Spain has been unsuccessful, the latter must be ordered to pay the costs of the proceedings.

On those grounds,

THE COURT (Fifth Chamber)

hereby:

1. **Declares that, by failing to adopt the laws, regulations and administrative provisions necessary to comply with Article 4(c) of Commission Directive 90/388/EEC of 28 June 1990 on competition in the markets for telecommunications services, as amended by Commission Directive 96/19/EC of 13 March 1996, the Kingdom of Spain has failed to fulfil its obligations under that directive;**

2. **Orders the Kingdom of Spain to pay the costs.**

Jann Edward La Pergola

Delivered in open court in Luxembourg on 7 January 2004.

R. Grass V. Skouris

Registrar President