Regulatory Policy and Creation of Regulatory Authorities in the Telecommunications Sector in Central and Eastern Europe

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A. Introduction

The enlargement process of the European Union to the Central and Eastern European Countries (CEECs) implies a political, economic and social transformation of the former socialist countries. According to the Copenhagen criteria of 1993, some crucial requirements must be fulfilled by the accession countries: the development of democracy (with emphasis on human and minority rights), the achievement of a functioning market and competitive economy and last but not least the capacity to implement the *acquis communautaire*.[1]

The introduction of competition in numerous sectors constitutes an essential part of the second (functioning competitive economy) and the third Copenhagen criteria (it is an important component of the *acquis*). At the European Community level, all the measures (derived from primary and secondary law) concerning the opening to competition of the telecommunications sector, constitute a steady and,

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[1] According to the Copenhagen criteria, accession will take place as soon as an applicant is able to assume the obligations of membership by satisfying the economic and political conditions required; i.e., that the candidate country has achieved: stability of institutions guaranteeing democracy, the rule of law, human rights and respect for and protection of minorities; the existence of a functioning market economy as well as the capacity to cope with competitive pressure and market forces within the Union; the ability to take on the obligations of membership (known as *acquis communautaire*, a concept embracing the primary and secondary law of the Community, as well as the case-law of the European Court of Justice), including adherence to the aims of political, economic and monetary union.

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at the same time, an evolutive part of the *acquis communautaire*.[2] Considering the situation only from the CEECs' perspective, almost all the writings analyzing the enlargement process[3] emphasize that accession to the EU represents an obvious net gain for the eastern economies as a whole, particularly with respect to the opening of numerous sectors to competition.

The introduction of competition in former State enterprises and in a large part of the network industries,[4] still subject to monopolistic structure, is particularly important. At first sight, the opening to competition could occur in an environment where 'deregulation' is a favoured concept. Nevertheless, it is not a chaotic process and it requires a new form of regulatory standards to be implemented by the State authorities. Moreover, governments that have opted for increased competition in telecommunications and/or privatization of until recently State-owned Public Telecommunications Operators have realized that these policies can only acquire the required effects if appropriate regulatory institutions are functioning effectively. The liberalization of the telecommunications sector in the transition countries could attract foreign and domestic private capital, which is a prerequisite for higher network development. This flow of capital could uphold the provision of the universal service obligation, which is a fundamental problem for a State or incumbent without financial means to achieve social goals.

This study aims at presenting an analysis of the role of the regulatory authorities in the telecommunications sector of the CEECs. The paper is limited to the examination of the developments in the telecommunications sector in the four CEECs known as the Visegràd countries: Hungary, Poland, the Czech Republic and Slovakia.[5]

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[2] Arts. 81, 82 and 86 of the Treaty (hereafter, article numbers will refer to the those introduced by the Treaty of Amsterdam). As regards secondary law, liberalization measures have been specified in directives stemming from Art. 95 (adopted by the Council) or Commission directives based on Art. 86.

[3] Many surveys and articles have been published showing that enlargement will be a win-win enterprise. *See* among others A. Mayhew, *Recreating Europe, the European Union's Policy towards Central and Eastern Europe* (Cambridge Cambridge University Press 1998) and a summary report by A. Inotai, 'Winners and Losers in EU Integration in Central and Eastern Europe' in (Nov. 1999) 6:4 Journal of Transforming Economies and Societies.

[4] By network industries, we understand sectors such as broadcasting, telecommunications, energy, post and certain transport services, relying on 'network' infrastructure. The majority of these sectors were, and in some cases still are, controlled by the State and entrusted with public service obligations in return for monopoly rights. *See* L. Cohen-Tanugi, 'Vers un droit européen des activités de réseau' in *L'Europe à l'epreuve de l'intérêt général* (C. Stoffaës (ed.)) (Europe ASPE 1994).

[5] After the agreement signed by Hungary, Poland and Czechoslovakia (which, since the disintegration of the country, has become the Czech and Slovak Republics) in December 1991. These countries were among the first to opt for a market economy structure, to enact competition laws and to undertake fundamental changes in their legal and economic regimes. Moreover, the choice of these specific countries tends to underline the new comprehensive Commission approach towards the enlargement process with the opening of

The article is divided into three parts. The first part of this paper examines the rationale for a new regulatory policy and the relevant *acquis communautaire* in the telecommunications sector. The second part considers the evolving legislative efforts in creating independent regulatory authorities in the CEECs. The last part of this paper consists of a short conclusion explaining the beneficial effect of promoting competition to the former State economies by means of creating a new regulatory framework. Ultimately the paper endeavours to indicate the importance of efficient and functioning regulatory authorities looking forward to the completion of the enlargement process.

B. The Regulatory Policy in the Telectommunications Sector – An Important Element of the *Acquis Communitaire*

The liberalization process implies the fostering of competition by opening the telecommunications sector to new entrants who can challenge the incumbent. Allowing entry and, consequently, private investments in the area, could not be done without strictly defined, binding legal provisions that can be litigated before judicial authorities. Therefore, liberalization requires regulation rather than deregulation. A new model of regulation is at stake in the telecommunications sector demanding the adoption of provisions to be implemented in a different legal environment, characterized by the ongoing process of liberalization, privatization and the creation of independent regulatory authorities.

I. Regulation of the Telecommunications Market

Despite the dominant reliance on market forces to promote economic efficiency and innovation through competition between operators in the actual context of globalization, some economic regulation is still needed either in order to avoid 'market failures' (economic regulation) or to account for social implications (social regulation).[6] In the framework of the former, one tends to maximize the economic efficiency by controlling market power. The latter set of rules is required to implement universal service obligations.

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the negotiations process with all the CEECs (as opposed to the former differentiation concept: Hungary, Poland and the Czech Republic were part of the first negotiations round, while Slovakia participated in the second).

[6] *See* Proceedings of the OECD/World Bank Conference on Competition and Regulation in Network Infrastructure Industries, Budapest 28 June–1 July 1994.

1. Economic Regulation

The concept of economic regulation refers to what Prosser has defined as a 'regulation for competition' and which involves 'creating the conditions for competition to exist and policing it to ensure that it continues to exist'.[7] With the advance of the liberalization process, the need for a new and more elaborate regulatory policy is more and more evident. While liberalization has paved the way for new entrants, the regulatory framework, which must 'perpetuate' open and fair competition, requires further sophistication. This feature can be applied to the developments that occurred in the CEECs analyzed in the 1998 EBRD survey.[8] As the survey points out, in the majority of countries, there is a lag between laws that allow new entrants and regulations that will foster the viability of new entrants within the telecommunications industry.

The role of new economic regulation could be taken care of by a package of sector-specific regulations, but it would also be possible to entrust this function to the existing competition rules. The case law of the European Court of Justice considered the application of national and EU competition rules acceptable in order to control market power in the telecommunications sector.[9] A similar approach was adopted by the Commission in the 1999 Communications Review, in which the Commission proposed a progressive phase-out of sector-specific regulation and its replacement by general competition rules. Such a solution could be acceptable for the CEECs, where the process of adopting general competition statutes in order to ensure the introduction of competition in different sectors of the economy has been the first fundamental component of their reforms.

It should not be forgotten that some sector-specific regulations are still missing in the transition countries. Switching to the application of general competition rules[10] could facilitate the legislative process and allow the CEECs to skip an important sequence of the liberalization process, undergone by the EU Member States. At first sight this approach appears attractive, but at this stage it is certainly not achievable in the CEECs. On the one hand, the shift to general competition provisions is considered possible once the telecommunications markets become more competitive and liberalization is advanced enough. This is not, as yet, the case in the transition countries. On the other hand, there is the seemingly unsuccessful example of New

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[7] *See* T. Prosser, *Law and the Regulators* (Oxford 1997).

[8] Which is a reasonable conclusion since the *acquis communautaire* has to be implemented by the CEECs and the countries pursue a similar path to liberalization of the telecommunications. *See* 'Market Perceptions of Telecoms Reform, Survey Results' in *Law in Transition* (EBRD 1998).

[9] Judgment of 20 March 1985 in Case 41/83, *Italian Republic v. Commission (British Telecommunications)* [1985] ECR 873.

[10] Provisions which present for the CEECs more or less an accurate reproduction of the original treaty articles dealing with competition, since all of them refer to Arts 81, 82, and 87 of the Treaty. Compare with the provisions of the Europe Agreements or the CEECs Competition statutes.

Zealand, where the government only considered general competition rules in order to create a competitive telecommunications market.[11]

The existing economic regulation refers in essence to production technologies (other than those linked with setting common technical product standards); eligible providers (granting and policing licences); terms of sale (i.e., output prices and terms of access); and standard marketing practices (e.g., advertising and opening hours).[12] The adoption of new regulatory instruments is a continuous process, which in parallel with the existing EU telecommunications framework justifies the substantial quantity of sector-specific regulation. As regards the existing regulatory provisions, the National Regulatory Authorities (NRA) in the CEECs have to supervise the implementation and enforcement of the EU legal instruments. This legislation refers to the provisions related to access to the market, prohibition of cross-subsidization (by means of separate accounting for the telecommunications activities), cost-orientation of prices, career selection and number portability requirements, and so on.[13] The NRAs are the principal enforcers of these regulatory schemes, covering both economic and social policy objectives.[14]

2. *Social Regulation is equally important for the CEECs*

In many parts of the world, concerns about universal service – guaranteed provision of service to everyone at an affordable price – has been used as an argument against privatization and liberalization.[15] To a certain extent, this statement remains true for CEECs where governments have not always enacted new legislation and speeded up the pace of the reforms in order to preserve, in practice, the rights of influential industrial groups. The official reason put forward is that privatization and subsequently de-monopolization would threaten the constant provision of services at an affordable price to all consumers demanding them, without discrimination as regards their geographic location.[16]

The concept of universal service was first used in the United States and more

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[11] For this and other examples of other countries, *see* M. Kerf and D. Geradin, 'Controlling Market Power in Telecommunications: Antitrust vs. Sector-Specific Regulation, An Assessment of the United States, New Zealand and Australian Experiences' in (1999) 14 *Berkeley Technology Law Journal.*

[12] *See* 'Relations between Regulation and Competition Authorities' (Roundtable OECD 1999).

[13] Directives adopted by the Council (based on Art. 95) and by the Commission (based on Art. 86(3)). Some of the Directives are cited below.

[14] *See* D. Geradin, 'Institutional Aspects of EU Regulatory Reforms in the Telecommunications Sector: An Analysis of the Role of National Regulatory Authorities' in (2000) 1 *Journal of Network Industries.*

[15] J.E. Stiglitz, 'Promoting Competition and Regulatory Policy: With Examples from Network Industries', speech delivered on 5 July 1999 at the World Bank, Beijing, China.

[16] These obligations respond respectively to the principles of universality, equality and continuity.

recently taken up by the European Commission. First mentioned in the Green Paper on Telecommunications,[17] it was legally introduced in Directive 95/62 on Voice Telephony, amended by Directive 98/10. The financing of the universal service is addressed by Directive 97/33, which also defines it as '... 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 practice, EU legislation defines universal service as comprising the provision of voice telephony services via a fixed network connection, which also allows a fax and a modem to operate, as well as the provision of operator assistance, emergency and directory inquiry services[18] and the provision of public payphones. The concept of universal service as defined by the EU legislation represents a minimum that Member States are free to exceed.[19]

Such types of social regulation are based 'on the desire to avoid an undesirable distribution of wealth and opportunity'.[20] One of the traditional arguments used to oppose liberalization has always been that universal service can only be provided by a monopolist. The incumbent can use the revenues from the commonly profitable market segment and the long-distance telephony in order to finance a less profitable segment, which is local voice telephony. One can clearly comprehend the objective of redistribution of benefits, which is sought after by applying the universal service provision. With the ongoing process of liberalization, incumbents argue that with their exclusive rights being phased out, they will be unable to honour their obligation to ensure affordable basic telephone service. Consequently, regulators must resolve the problem by finding an effective way of guaranteeing the universal service provision. Two possible approaches are specified in the EU telecommunications legislation, dealing with the financing of the universal service:[21] the creation of a fund or the ability to impose on competing operators the payment of direct additional charges added to the price for interconnection.

The Commission in its Fifth Report on the Implementation of the Telecommunications Regulatory Package mentions the possibility for Member States to set up a universal service fund,[22] but the transition countries might follow another direction. The CEECs have to ensure the affordability of the universal service, guaranteed by

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[17] *See* Commission Communication COM(87) 290 of 30 June 1987.

[18] Including the provision of subscriber directories.

[19] *See* Commission Communication of 26 September 1996, Services of General Interest in Europe, OJ 1996 C281/3. For a thorough analysis of this point refer to D. Geradin, *The Liberalisation of State Monopolies in the European Union and Beyond* (2000) at p. 197.

[20] *See* T. Prosser, *supra* note .

[21] *See* COM(96) 608.

[22] *See* Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions, Fifth Report on the Implementation of the Telecommunications Regulatory Package, COM (1999) 537. However, Member States do not have the obligation to create a fund and until now only France has set one up.

measures adopted by the National Regulatory Authorities. The lack of full competition in the market could lead to an initial temporary increase in prices. However, it can be assumed that in the long-term, competition will make prices decrease. In this respect, it is important to mention that the new regulatory framework in the EU, which is effective from 1 January 2002, proposes one specific directive that addresses services of general interest, namely 'universal service and users' rights relating to electronic communications networks and services.[23]

II. The Missions Entrusted to the Regulatory Authorities

Views do not always concur as regards which tasks should be entrusted to the regulatory authorities. The regulators' mission in each country might vary according to the different outcomes the regulator is mandated to achieve. However, it is more or less universally accepted that NRAs must be liable as regards some core functions such as are defined in several EU harmonization directives.[24]

- **Network interconnection** – it is important to set up effective conditions for new competitors to enter the market. This peculiar feature of the telecommunications sector should be underlined, where access to the market for a new competitor is based on its fruitful co-operation with its 'worst' competitor: the incumbent operator. In practice, the regulator must determine the specific modalities of interconnection in order to provide transparent and non-discriminatory access to the new operators, as well as the appropriate levels of charges for interconnection. The interconnection rules to be implemented in the CEECs require, first, the adoption of a set of principles governing the interconnection, secondly, procedures and processes to make regulatory decisions in specific cases, and thirdly, mechanisms for monitoring compliance and enforcement.[25] The Interconnection directive presents a thorough overview of the technical aspects and the regulatory commitments to be carried out as regards interconnection requirements.[26]
- **Controlling access to the market** – NRAs are responsible for the enforcement of the condition attached to various licensing and authorization procedures. In

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[23] *See* Communication from the Commission–Services of General Interest in Europe, COM/2000/0580.

[24] Directive 90/387 on the establishment of the internal market for telecommunications services through the implementation of open network provision, O.J. 1990, L 192/1 and the subsequent amending directives.

[25] *See* Jürgen Müller, 'International Experiences in Competition and Regulation in Telecommunications Industries', paper delivered at OECD/World Bank Conference on Competition and Regulation in Network Infrastructure Industries, Budapest 28 June–1 July 1994.

[26] Directive 97/33 on interconnection in telecommunications with regard to ensuring universal service and interoperability through application of the principles of Open Network Provision (ONP), OJ 1997 L 199/32.

this respect, the role of the NRAs varies from one Member State to the other.[27] The licensing function may be unnecessary or minimal in other countries (as in New Zealand or the United States long-distance market). In order to ensure the transition from monopoly to competition of the telecommunications sector, it is important to define strictly the conditions assigned the operators in their licences, and in particular, the commitments entrusted to the incumbent's licence. The regulator must monitor the accounting of the incumbent (as well as that of the other operators) to ensure that tariffs and interconnection charges are cost-orientated, to prevent cross-subsidization and to safeguard consumer interests.[28] All these issues are particularly important in the CEECs where promoting competition is a recent process, which still encounters problems and internal opposition.

- **Promoting social goals by implementing the universal service obligations** – NRAs must ensure the provision of affordable services to some categories of consumers. This might include low-income households, disabled persons or people living in remote geographic areas. The regulator should determine the manner of financing the universal service obligations in order to compensate the incumbent or the operators in charge of the provision for the losses incurred. Such a commitment, together with a more general protection of consumer interests and the consideration of potential user complaints, emphasizes the important task entrusted the regulator in the particularly difficult social and economic transition in the CEECs.
- **Dispute resolution** – dispute settlement between telecommunications operators, as well as between operators and end-users is a responsibility that requires the involvement of the regulatory authorities. This is an important issue, particularly in the case of the CEECs, which encounter many difficulties in the initial stages of the liberalization process, for the most part concerning access and interconnection. The most efficient way to resolve this kind of problem requires the creation of a strong and independent telecommunications regulator who has the power and the knowledge to impose binding decisions.

In order to open markets to effective competition, the EU regulatory framework requires Member States to ensure the effective separation of regulatory and State ownership functions. The NRAs have an extremely important role for the full implementation of the EU regulatory framework, which will allow the achievement of the Lisbon Strategy. The objective set by the Lisbon European Summit in 2000 is that the European Union should become the most competitive and dynamic knowledge-based economy in the world.

The CEECs endeavour to achieve a rapid accession to the EU. In order to comply with the *acquis*, they are required to implement effectively the EU regulatory

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[27] *See* D. Geradin in *Journal of Network Industries, supra* note 14 (at p. 16).
[28] 'Telecommunications Legal Reform' in (1998) *Law in Transition.*

framework liberalizing their telecommunications services and ensuring the independent functioning of their NRAs. In the following part, the issues as regards the fulfilment of the latter condition are analyzed.

C. The Establishment of Regulatory Authorities in the CEECs

As mentioned above, the CEECs have initiated significant reforms in order to set up market-based and competitive economies. In this context, new legislation was required so as to comply with the Copenhagen criteria. Liberalization by means of de-monopolization of the former natural monopolies, together with privatization, represents the main tendencies of the new regulatory schemes.

Alongside this process is the creation of the new regulatory authorities, whose activities should in particular control market access[29] and promote competition. The first national telecommunications policies of the transition countries dealt mainly with the restructuring of the incumbent operators. In contrast, one of the main objectives of the most recent programmes is the establishment of a transparent regulatory framework and the creation of independent regulatory authorities.[30]

Instead of traditional regulation performed by the State administrative bodies, the regulatory powers are to be carried out by independent entities, no longer controlled by the State. EU legislation requires the implementation of the *acquis* in this sector, which is analyzed in the first subsection of this part. Despite efforts to establish efficient and independent institutions, working for the completion of the liberalization process, progress is uneven in the Visegràd countries and uncertainties still remain.[31] The developments in the CEECs will be treated in the second subsection of this part.

I. Taking into Consideration the EU Legislation

1. The 'independence' requirement

In the EU, the requirement for independent telecommunications regulators is expressed in the relevant Directives, which insist on the strict division between regulatory and operational functions.[32] This requirement for 'independence' can also

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[29] Art. 7 of the Directive 90/388, OJ 1990 L 192/10, known as the 'telecommunications services' Directive.

[30] *See* Basic Principles of Telecommunications Policy of the Czech Republic.

[31] *See* Summary Progress Report, EU-CEEC Joint High Level Committee, European Ministerial Conference, Warsaw, 11-12 May 2000, p. 15.

[32] *See* Art. 7 Directive 90/388, OJ 1990 L 192/10, and the subsequent Directives on voice telephony and interconnection.

be found in the case-law of the ECJ.[33] However, it is only recently that this requirement was developed and made explicit. According to some amended EU instruments, the independence of the NRA can be guaranteed if the authority 'shall be legally distinct from and functionally independent of all organizations providing telecommunications networks, equipment or services'.[34] The second tool to ensure independence pursued by the directive refers to the Member States that retain ownership of or a significant degree of control over organizations providing telecommunications networks and/or services. Member States must ensure effective structural separation of the regulatory function from activities associated with ownership or control. The purpose of the EU legislation is clear: the above-mentioned provisions must ensure, by means of the required legal separation and functional independence, that:

- the regulator and the incumbent operator may not share personnel and/or facilities; and
- the regulator may not perform any tasks associated with the representation of the shareholders or the management of the incumbent operator.[35]

If the operator is still a public monopoly, the regulator should remain independent from the State acting as an owner. These clarifications are needed because of the existing links between the bodies (despite the legal separation), such as a continuous transfer of personnel, the sharing of various facilities, and so on. The 'independence' requirement is, therefore, a part of the *acquis communautaire*, and consequently, the CEECs must incorporate it into their internal legislation.

2. *The 'accountability' requirement*

Another important issue regarding setting up regulatory authorities in the CEECs and related to the 'independence' criterion, required by the EU legislation, is how to establish a balance between, on the one hand, democratic accountability of the regulatory body,[36] and, on the other, its decision-making independence.[37] As Jacobs notes, some OECD countries (for instance the United States and the United Kingdom) have created independent regulatory bodies whose management is

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[33] *See, inter alia*, Judgment of 19 March 1991 in Case C-202/88, *French Republic v. Commission of the European Communities*, [1991] ECR I–1223; Judgment of 27 October 1993 in Case C-69/91, *Criminal proceedings against Francine Gillon, née Decoster*, (1993) ECR I–5335, etc.

[34] Article a §2 of Directive 90/387 as amended by Article 1 §6 of Directive 97/51, OJ 1997 L 295/23 the 'Amendment ONP Framework Directive'.

[35] *See* 'The Building Blocks for Telecoms Reform' in (1998) *Law in Transition*.

[36] Political control exercised by the Parliament for example.

[37] For a more thorough analysis, see S.H. Jacobs, 'Building Regulatory Institutions in Central and Eastern Europe', paper prepared for the OECD/World Bank Conference on Competition and Regulation in Network Infrastructure Industries, Budapest, 28 June–1 July 1994.

sheltered from the influence of the political authorities. In other countries (such as Germany), regulatory authorities are placed within ministries, raising doubts as to their political independence.[38]

Another approach has been adopted in New Zealand where the telecommunications sector is only 'regulated' through general competition law, but without great success.[39] An approach often envisaged in the OECD countries is the establishment of specialised and expert regulatory agencies,[40] set up before privatization and limiting the opportunities for government intervention.[41]

The balance to be found between independence and accountability might be achieved through the guaranteed possibility to challenge the decisions of the NRA, which represents a fundamental right of every citizen. It is of particular importance for the CEECs to ensure the enforcement of this fundamental aspect of the rule of law criterion. The decisions of administrative authorities have to be subject to judicial review, although the modalities can differ depending on the judicial structure of the country. As regards EU legislation, Member Sates are requested to set up an appeals procedure which a party affected by the decision adopted by a NRA can use to have that decision reviewed.[42]

In order to attract investors to the CEECs, it is necessary to offer them guarantees as regards the precarious environment of the reform process. A transparent regulatory framework must be adopted providing for clear guidance on the criteria to be used for reaching a decision. Such frameworks cannot be changed arbitrarily by other administrative acts, such as ministerial decrees. Legal remedies must be established in case of infringements and breaches of law must be listed and explicitly defined.

3. The institutional structure of the NRAs

There is one controversy surrounding the structure of the regulatory authority in the CEECs. Should regulatory bodies specialize and regulate solely in one sector (for

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[38] However, it has to be mentioned that in Germany the NRA is an agency under the supervision of the Minister of Economic Affairs, while the State's shareholding in Deutsche Telecom belongs to the Ministry of Finance, thereby ensuring separation from the regulatory function. For a thorough analysis of these questions, *see* Fifth Report on the Implementation of the Telecommunications Regulatory Framework, Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions.

[39] For this and examples of other countries, *see* Kerf and Geradin, *supra* note , and 'Phare Multi Country Programme' prepared by Eurostrategies for the European Commission, The Development of a National Regulatory Authority, June 1997, at p. 15.

[40] *See* Jacobs, *supra* note 37 at p. 309.

[41] This commendation is given by World Bank experts, not realized in the CEECs, where the privatization process has started first; *see* P.L. Smith and B. Wellenius, 'Mitigating Regulatory Risk in Telecommunications' in (July 1999) *Public Policy for the Private Sector.*

[42] *See* Directive 97/51, Article 5a §3.

instance telecommunications or energy)? Or is it better to establish cross-sector regulators? Besides the core requirements analyzed above, EU legislation leaves a large discretionary margin to Member States as regards the institutional structure of their NRAs, as well as the powers and competencies entrusted to the regulators, which explains the different options chosen.[43]

An advantage of cross-sector regulators is that they appear to be less vulnerable to 'capture' by regulated industries.[44] The regulator should not favour one operator over another. In order to avoid such behaviour, it is important that the regulator is not involved in the adoption of commercial decisions on behalf of the regulated companies. One has to agree that a multi-sector agency is less likely to be captured by one specific company or, to take a scenario differing from the concept of regulatory capture, to be controlled by a sector-specific ministry or administration.[45] An advantage favouring cross-sector regulation for the CEECs is the fact that often transition economies cannot afford the finance and human resource costs of a separate regulatory agency for each sector. Nevertheless, setting up a cross-regulator is not the common approach opted for by the Visegràd countries, as we shall see in the analysis that follows.

According to the European Commission, four models of regulatory authority are conceivable for adoption in the CEECs.[46]

- **A Department within a Ministry** – through the establishment within the Ministry for Communications of a Department responsible for regulatory matters. The advantage for the CEECs is that this is the least costly approach, which is not without importance for transition economies. This option could be convenient as regards the provision of universal services (because some political control concerning this issue is retained), an aspect of particular importance in the CEECs operating difficult and socially sensible reforms. The disadvantage is that it leaves the control and regulation of the sector open to political influence.
- **A semi-autonomous entity within a Ministry** – this model is not common but did exist in France, where prior to the creation of a fully independent regulator, there was a Directeur de la Réglementation Générale. In such cases, the relationship between the Director and the Minister must be clearly defined, in

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[43] *See* D. Geradin, in *Journal of Network Industries*, *supra* note 14.

[44] '... a generalised enforcement agency, such as an anti-monopoly authority, will be less susceptible to regulatory capture than a (specialised) regulatory agency; the staff and management of the former must deal with a variety of industries and interests on a day-to-day basis and are likely to develop neither the rapport nor the institutionalised interdependence with the regulated industry that may develop under the latter,' *see* J.A. Ordover and R. Pittman, 'Competition Policy for Natural Monopolies in a Developing Market Economy', paper prepared for the OECD/World Bank Conference on Competition and Regulation in Network Infrastructure Industries, Budapest, 28 June–1 July 1994.

[45] *See* Smith & Wellenius, *supra* note .

[46] Phare Multi Country Programme, *supra* note 39 at p. 15.

order to avoid political interference of the latter as regards the decisions of the former.

- **An independent semi-autonomous regulator** – this model is applied in the United Kingdom, where under the Telecommunications Act of 1984 the Office of Telecommunications (OFTEL) was created as an independent, non-ministerial Department. Its independence is secured basically through the limitation on the Secretary of State for Trade and Industry to demand the resignation of the Director-General for reasons other than incapacity or unlawful behaviour. The budget of OFTEL is adopted by Parliament. As more and more countries opt for this approach, one could recommend its adoption to the CEECs as far as the equilibrium between the policymaking body (Ministry) and the regulator dealing with day-to-day control of the sector could be clearly defined in the legislation.
- **An independent autonomous regulator** – the main example being the Federal Communications Commission in the United States, responsible for telecommunications, radio communications and broadcasting. It is created by and subject to the law only and completely independent from the respective ministries and administration authorities.

As mentioned above, the creation of the Regulatory Authority is a part of the *acquis* and must be carried out in the CEECs. The NRA may initially be a part of a Ministry (in this case, the 'independence criterion' must be monitored). Nevertheless, the Commission considers there should be a determination to create an independent regulator within five years of the liberalization process and the adoption of the new telecommunications legislation.[47] One could argue that as the liberalization process advances further, more responsibilities should be given to the regulatory authority in opposition to the Ministry. Another problem as regards the setting of the regulatory authorities in CEECs would be adequate resourcing. Experienced staff with pertinent professional knowledge must be trained and appropriate funding has to be provided in order to retain the personnel.

The feature that must be stressed at this stage is that the flexibility of the EU's regulatory regime will allow candidate countries to implement the *acquis* in the telecommunications sector by adapting it to domestic circumstances. This is particularly important for transition economies, which are still experimenting with some market mechanisms and must adopt truly new legislation in many sectors of the economy in order to make it competitive while responding to the accession criteria.

II. Regulatory Authorities in the Visegràd Countries

1. The Czech Republic

The new Telecommunications Law in the Czech Republic provides for:[48]

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[47] Ibid. at p. 21.

[48] Act on Telecommunications 151/2000, which entered into force on 1 July 2000.

- conditions for establishing and operating telecommunications equipment and telecommunications networks;
- conditions for providing telecommunications services; and
- regulatory issues.

Regarding this last point, the principal institutions which carry out regulation in the telecommunications sector, provided for in the new Telecommunications Law,[49] are the Ministry of Transport and Telecommunications on the one hand, and the Czech Telecommunications Office, on the other.[50] The Ministry is responsible for telecommunications policy and the adoption of the main rules and principles of State regulation in telecommunications, international relations and fulfilment of international obligations, as binding to the Czech Republic. Moreover, it approves the frequency allocation. The Czech Telecommunications Office is expected to perform the day-to-day executive activities connected with the regulatory framework provided for by the Telecommunications Law.[51]

This authority is established as a State administrative body funded by the State budget. The nomination procedure for the President of the Authority and the preparation of its statute are proposed by the Minister of Transport and Communications and approved by the Government.

In the author's opinion, this measure contradicts the 'independence' requirement of the regulator from the State acting as an owner (taking into consideration the fact that the privatization process of the incumbent operator is not yet complete). The European Commission expressed concerns about alignment of the new law with the *acquis* as regards the complete separation of the regulator from the Ministry.[52] As the Commission points out, the government has announced its intention of disposing of the State's remaining shareholdings in operating companies, which will diminish the importance of the separation aspect. However, until it happens, the presence of senior officials from the Ministry of Transport and Communications in the supervisory boards of operating companies infringes the separation of functions required by the *acquis*. According to the Commission, the remaining problems regarding the alignment with the *acquis* concern, in particular, the separation of regulatory and operational functions, cost-orientation of tariffs, asymmetric

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[49] Article 3 of the new Czech Telecommunications Law.

[50] Refer to the Supplement to the previous document National Telecommunications Policy of the Czech Republic.

[51] State of Telecommunications in the Czech Republic, Main Documents and Legislation, at <http:/www.mdcr.cz/archiv/telecomunication14100.htm>.

[52] Regular Report from the Commission on the Czech Republic's Progress towards Accession, 8 November 2000. The same critics persist in the last Commission's Regular Report on the Czech Republic's Progress towards Accession, 13 November 2001 (see p. 79), where the Commission points out that: 'The Ministry of Transport and Communications retains significant powers of a regulatory nature. It is inconsistent with the principle of separation of regulatory and operational functions for Ministry officials to be involved in any way in the managerial or supervisory boards of operating companies or in their

regulation and availability of carrier selection facilities. It is urgent that these issues be resolved in order to proceed with opening the market and to achieve effective competition and adequate consumer protection.

2. Hungary

Hungary established a National Communications Authority (HIF) in 1993, which was the first independent agency in the Visegràd countries with budgetary autonomy. Between 1993 and 1995, it was called Telecommunications General Inspectorate, an administrative body under the control of the Ministry for Transport, Telecommunications and Water Management. Subsequently, as a result of the transformation of the Inspectorate into the Communications Authority of Hungary, greater autonomy of the regulator has been achieved.[53] Since June 2000, the responsibility for the telecommunications sector has been transferred from the Ministry to a Government Commissioner within the Prime Minister's Office. The Commissioner is in charge of telecommunications regulation, governmental informatics, the information society and postal services and the HIF reports to him.

In this context, the HIF prepares new regulations or amendments to existing legislation, participates in the approximation of the Hungarian legislation to the *acquis*, prepares concession agreements and holds a register of tenders and agreements and plans. Last but not least, the HIF and its regional communications inspectorates are expected to ensure market monitoring and quality reviewing.[54]

Regulatory capture is evidenced by an institutional bias of the regulator in favour of the dominant operator. One of the reasons is that before privatization, the incumbent MATAV was integrated within the governmental bureaucracy. This facilitates MATAV to resist formal regulatory change and to manipulate the flow of information to the regulator, as the limited resources of the latter do not allow him to penetrate such a complex business and operational structure.[55] It is safe to presume that similar problems exist in other CEECs whose regulatory bodies in telecommunications tend to be even less independent than the one in Hungary.[56]

The most important task of HIF was the preparation of the new Communications

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privatisation.'

[53] The structure of the regulator, as well as the approach of the Hungarian government towards privatization of the incumbent and other public utilities, have been influenced by the choices made by the British government. In this respect, *see* 'Linking Privatisation and Regulatory Reform' in (1998) *Law in Transition.*

[54] *See* Government Decree No. 142/1993 on the establishment of the Uniform Communications Authority.

[55] *See* 'Linking Privatisation and Regulatory Reform' in (1998) *Law in Transition.*

[56] In this respect, by deciding to sell the whole of the State's shareholding in the incumbent operator, Hungary avoided some problems that often arise because of the lack of clear separation of the State as regulator from the State as telecommunications operator. *See* Commission's Regular Report on Hungary's Progress towards Accession, 13 November 2001, at p. 70.

adopted in 2001.[57] The Act tends to ensure a unified framework complying with EU standards as regards the fundamental issues in telecommunications, postal and information services that have to date been separately handled. The HIF must be restructured to take account of the recently enacted law. Some other changes are required to establish an appropriate legal framework for the liberalized communications market and to ensure that regulation of the market fully satisfies the requirements of the *acquis* in this sector.[58]

3. *Poland*

Previously the Polish Ministry of Posts and Telecommunications was responsible for telecommunications policy and regulation and acted as a National Regulatory Authority. The ownership functions of the national operator TPSA being performed by the Ministry of the Treasury, separation between the regulating and operating status was achieved from the outset. Nevertheless, this situation was not accepted as satisfying EU requirements as regards independence of the regulatory authority.

This explains why, in the new telecommunications law, an independent self-financing National Regulatory Authority is being set up (called the Office of Telecommunications Regulation).[59] The new law, enacted in July 2000, entrusts this legal body with broad powers to regulate the sector.[60] Currently, the Polish NRA is fully functioning as a separate independent legal body.[61] However, problems continue to exist. As the Commission indicated in its last report on Poland's progress towards accession:

> The foundations laid by the Telecommunications Act now need to be built on to secure complete compliance with the *acquis*, particularly regarding cost-orientation, local interconnection, affordability, universal service and the availability of carrier selection and number portability facilities. Further progress is now needed with the remaining pieces of secondary legislation that are necessary for the market to be regulated properly and fully opened. Much of the success of the reform of the telecommunications sector will depend upon

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[57] Act XL of 2001 on Communications. As regards the Communications Authority, refer to provisions in Ch. X, Arts. 70–74.

[58] Commission's Regular Report on Hungary's Progress towards Accession, 13 November 2001, at p. 71.

[59] *See* the Telecommunications Law, S. VII, Ch. 1, Art. 110.

[60] Regular Report from the Commission on Poland's Progress towards Accession, 8 November 2001.

[61] Commission's Regular Report on Poland's Progress towards Accession, 13 November 2001, p. 76. The Commission points out that by mid-2001 the new body had succeeded in ensuring that the competing long distance services for which licences had been granted in 2000 were able to operate in practice.

the NRA continuing to improve its capacity to oversee and regulate the sector in an efficient and independent manner.[62]

4. Slovakia

Precedent legislation in Slovakia charged the Telecommunications Office and the Regional Telecommunications Offices with the responsibility to act together as a regulatory body. These entities were State administration authorities acting under the supervision of the Ministry of Transport, Posts and Telecommunications. The Telecommunications Law, in force since July 2000, envisaged the establishment of a National Regulatory Authority as a separate legal body with wider powers and greater independence to regulate the sector and to administer the radio spectrum, thus allowing Slovakia to comply with the requirements of the *acquis*.[63] The Telecommunications Office was established in 2001. A large number of existing telecommunications licences have been reissued under the new Act on Telecommunications and the NRA organized its new authority in relation to the pricing of telecommunications services.[64] The Ministry of Transport, Post and Telecommunication retains legislative and policy-making functions. In this respect, the Commission points out that in order to achieve a proper separation of regulatory from operational functions, the Ministry should no longer exercise the State's proprietary rights in the incumbent sector.[65]

The NRA is financed through the State budget. A model of co-funding from the fees for regulatory performance could be provided later depending on the economic situation in Slovakia. The Chairman of the Telecommunications Office is nominated by the Government and appointed by the Parliament. It is important to safeguard the independence of the NRA, as well as to establish close co-operation with the competition authority, which has also been working in the telecommunications field.

5. Concluding remarks

The issues mentioned above do not present a comprehensive analysis of all the problems that can be found in the context of the adoption of adequate regulatory policies and the creation of telecommunications regulatory authorities in the Visegràd countries. Also, the analysis does not contain an exhaustive description of all typical problems legislative process in the transition countries. However, the adoption of the new Telecommunications Acts by the CEECs provides good

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[62] Commission's Regular Report on Poland's Progress towards Accession, 13 November 2001, at p. 77.

[63] Regular Report from the Commission on Slovakia's Progress towards Accession, 8 November 2001.

[64] Commission's Regular Report on Slovakia's Progress towards Accession, 13 November 2001, at p. 71.

[65] Ibid.

examples for key issues in the liberalization process and the efforts to achieve full compliance with the *acquis communautaire*. The first national telecommunications policies of the transition countries dealt mainly with the restructuring of the incumbent operators. In contrast, as already mentioned, one of the main objectives of the new telecommunications legislation in the CEECs is the establishment of a transparent regulatory framework and the creation of independent regulatory authorities.[66]

At the time of writing, it is not possible to evaluate the effectiveness of the newly created independent regulatory authorities in the Visegràd countries. Some conclusions are nevertheless discernible. The four countries examined adopted new telecommunications legislation, providing for the creation of independent regulatory authorities. The practical implementation is underway. The cross-regulation structure is not the common approach opted for by the Visegràd countries, despite some advantages described above. Independence and accountability criteria are generally observed (the exceptions were discussed in this paper). In a short period of time, a more specific assessment of the efficiency of the NRAs should be possible.

D. Conclusion

In a *Market Trends* commentary, published in the first release of its web-based tracking service New Entrants: Central and Eastern Europe, Analysis argues that competition in the CEE fixed telecommunications market is being impeded by the slow progress in establishing independent regulatory authorities.[67] The authors consider that in most transition economies, governments have focused on privatizing the incumbent in order to raise much-needed capital. They have therefore been unwilling to take action that could have decreased the value of incumbent telecommunications operators in advance of the sale (such as rapid liberalization). This has tended to include a reluctance to introduce a regulatory framework promoting competition and regulators with effective powers.

Nevertheless, the governments of the CEECs have made a comprehensive commitment to comply with the requirements of the *acquis*. Liberalization and a functioning market economy are prerequisites in the perspective of accession of these countries to the Union. It has been proven that competition leads to more effective and optimal allocation of resources, lower prices and larger choice for consumers and increased efficiency in general. It is impossible to benefit from these advantages in the framework of a monopolistic structure because of the presumed tendency of monopolies to seek greater profits by creating an artificial shortage or by fixing inflated prices detrimental to consumers.

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[66] *See* Basic Principles of Telecommunications Policy of the Czech Republic.
[67] Analysis can be found at <http://www.analysis.com>.

Once the decision to liberalize is taken, there is an obvious need to adopt and implement[68] a new regulatory framework and to establish an independent regulator with no affiliation with the incumbent. Because of the risk of regulatory capture, it cannot reasonably be expected that competition will occur when the regulatory body serves the same interests as the dominant operator.[69] Independence from political interference is also necessary and that is the reason why it is preferable for the regulatory authorities to be functionally independent of governmental institutions such as ministries.

As can be observed, the Visegràd countries have pursued a similar path to liberalization. The same result is expected as regards the adoption of the regulatory framework and the creation of the NRAs. As already mentioned, the flexibility of the EU's regulatory regime (as to the institutional structure of the regulatory authorities) will allow candidate countries to implement the *acquis* in the telecommunications sector by adapting it to domestic circumstances. However, it must be emphasized that no flexibility is tolerated as regards the basic principles of regulation and complete opening of the telecommunications market. The CEECs have to pursue the reforms in order to achieve full compliance with the *acquis*. This is the only way to achieve successfully rapid accession to the EU.

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[68] It should be noted that EU legislation is rapidly adopted in the CEECs, but the implementation process has been much more difficult.

[69] *See* 'Market Perceptions of Telecoms Reform, Survey Results' in (1998) *Law in Transition*.