

**The national politics of European regulation: institutional reform in telecommunications**

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**Paper presented to the 6<sup>th</sup> biennial conference of the European Community Studies Association, Pittsburgh, June 1999**

  
**The national politics of European regulation: institutional reform in telecommunications**

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Whilst regulation constitutes the core activity of European integration (Majone 1994, 1996) and is enforced through the supremacy and direct effect of EC law (cf. Stone Sweet; Weiler), the EC largely relies on alteration of national rules, procedures and organisations. Although most debate has focused on how and why European policies/regulation have developed (cf. Sandholtz and Stone Sweet 1998; Wallace and Wallace 1996; Moravcsik 1993, 1997,; Marks 1997; Marks et al 1996; McGowan and Wallace 1996, Richardson 1996), the impact of the EC on its member states therefore represents an essential part of analysis of European integration.

EC regulation can have several different types of impact, affecting, for example, market structures, economic performance, ideas and processes of decision making. The present paper examines its effects on the reform of formal rules and organisational arrangements in member states. These effects provide a good test of the impact of European Community/Union regulation for three major reasons. First, most EC regulation takes the form of formal rules, that must then be implemented at national level. Formal/legal 'institutional arrangements' are visible and given that the EC acts primarily through legal requirements, are the areas where maximum impact can be expected; hence if the EC is found to have little influence on formal institutions, a priori, it may have even less effect on more culturally-rooted practices for which the EC has even fewer policy instruments. Second, national institutions have been claimed to be stable and highly resistant to change, being rooted in differing national histories (Hall 1986; Immergut 1992; Weir 1992; Hattam 1993; Steinmo 1993; Dobbin 1994). They change slowly and/or very rarely, at times of crisis (Thelen and Steinmo 1992; Krasner 1984). Thus if European regulation leads to changes in long-standing domestic institutions, then its impact can be assessed to be

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<sup>1</sup> The present paper was written during a Jean Monnet Fellowship at the Robert Schuman Centre, EUI; the author expresses his gratitude to the RSC.

considerable. Third, if 'institutionalist' explanations of policy making are valid, modification of domestic institutions due to EC regulation should then strongly influence the strategies and roles of actors in national decision making and markets.

Assessing the impact of EC regulation is far from easy, as a single factor must be disentangled from the many influences on institutional reform. Nevertheless, certain questions can be posed to guide analysis. One is the extent to which EC requirements were novel for member states, representing evidence that the EC might be leading change, or whether EC rules were following existing national arrangements, suggesting that EC regulation was merely validating arrangements already established at the national level. Another concerns the forms and mechanisms whereby EC regulation influenced national institutional reform. A third issue is what other factors were involved in the modification of institutions in member states and the ways in which EC regulation interacted with such factors. Hence, for example, the ways in which the EC entered national reform debates, the uses made of the EC by actors in the policy process and the interplay between EC requirements and other factors, can be studied. Finally, and most difficult, the relative importance of EC regulation and other influences for change needs to be considered.

The present article looks at a case study: telecommunications, and compares the impacts of EC regulation on institutional reform in four countries: Britain, France, Germany and Italy. Telecommunications offers a particularly suitable example to look at the influences of the EC on institutional reform: EC regulation developed from modest origins in the mid-1980s into an extensive regime covering most of the sector by the late 1990s (Thatcher 1997; Scott and Audéod 1996, Sauter 1995, 1997, Natalicchi 1999), permitting analysis of 'before and after', as well as a sufficient time period for study; institutional reform was at the centre of policy debates in the sector and change was a visible and contested process; the four countries had national differences that permit appreciation of the various mechanisms whereby the EC could affect institutional reform, together with the limits on the EC's roles. More generally, telecommunications has been at the heart of national debates about industrial policy and restructuring the state (V Schmidt 1996, 2000).

The article, therefore, begins by briefly setting out the national institutional structures that existed before the mid-1980s in telecommunications and the main pressures for change, before looking at the key features and requirements of EC regulation most relevant to institutional reform (sections I and II); the purpose is not explain the development of national institutional arrangements or EC regulation, but to set them out in order to allow analysis of the impact of the latter on the former. The paper then compares alteration of two key institutional arrangements: competition; organisational structures, including ownership and regulatory bodies and power (sections III and IV). The concluding section seeks to link the findings to more general arguments about the impacts of EC regulation and the factors that influence those impacts.

### **I The terrain for EC action: national institutional structures by the mid 1980s and pressures for change**

Many formal institutional features of telecommunications were similar in Britain, France, Germany and Italy before the 1980s (Foreman-Peck and Müller 1988).

Publicly-owned PTOs (public telecommunications operators) held monopolies over the building and operation of public telecommunications networks and the supply of almost all telecommunications services and customer premises equipment in each country. The PTOs were the Post Office in Britain, the DGT (Direction générale des télécommunications) in France, the Deutsches Bundespost in West Germany. Italy differed somewhat in having fragmented supply, with several publicly-owned PTOs; the largest PTO was the ASST (l'Azienda di Stato per Servizi Telefonici). Most PTOs formed part of the civil service and were linked to postal services, being units within PTT (Post, Telegraph and Telephone) ministries;<sup>2</sup> Britain after 1969 was an exception, as the Post Office ceased to be a government department and became a public corporation, with its own legal identity. Users had almost no legal rights and there were no independent regulators for telecommunications: the PTT Ministries combined the functions of suppliers, national regulators and policy makers. Indeed, the concept of 'regulation' was rarely applied to telecommunications in Western Europe.

Many of the central institutional features were long-standing, dating from the early twentieth century. Periodically, significant debates about institutional reform arose in the four countries. The linkage of postal and telecommunications services and the organisational position of PTOs as part of the civil service, were periodically called into question (cf. Thatcher 1999b; Libois 1983; Werle 1990; Grande 1989). PTO monopolies over advanced services and certain forms of CPE were criticised, especially by large users of sophisticated services and firms straddling the computer and telecommunications markets. However, efforts at reform faced serious opposition, notably from trade unions, the political left and the nationalist Right. As a result, few institutional changes were introduced during the 1970s. In the early 1980s, reform processes began, but were largely confined to Britain, where after 1979, the Conservative governments began liberalisation and restructuring the state.<sup>3</sup>

However, traditional institutional frameworks in the four countries faced increasing transnational and domestic pressures for change; these began in the late 1960s, but became much stronger in the 1980s and 1990s. Technological and economic developments transformed telecommunications, notably the application of computing to the sector, new more efficient network equipment and falling costs (Stehman 1995; Thatcher 1999b; Vickers and Yarrow 1988). As a result, entry and competition became easier, undermining monopolies. At the same time, demand for telecommunications grew and became more diverse; hence a wider range of services was required and the effects of inadequate supply were more significant. Reforms in the United States offered an example of reform and also triggered lobbying by American policy makers and suppliers; in particular, liberalisation of services and CPE and the breakup of AT&T in 1984 led to challenges to national monopolies in Europe (Hills 1986). New ideas emerged, particularly in the United States, concerning the benefits of competition and the dangers of regulatory capture (Baumol et al 1982;

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<sup>2</sup> Or Ministries incorporating them; for ease of reference, they are referred to as PTT Ministries.

<sup>3</sup> Competition was introduced and in 1984 a majority of shares in BT were sold, BT was to operate under a licence and a new semi-autonomous sectoral regulator, the Office of Telecommunications (OfTel), was established (Thatcher 1999b).

Stigler 1971, Peltzman 1976, Kolko 1977). A fourth factor for change was the development of EC regulation, the focus of this paper.

Thus the impact of EC regulation must be assessed from a starting point in the mid-1980s of long-standing national institutions facing non-EC sources of pressures for change. At the same time, considerable obstacles to institutional reform existed and had largely prevented major organisational alterations in France, Germany and Italy.

## II Institutional aspects of EC regulation

Until the mid-1980s, the EC played almost no role in the regulation of telecommunications (Sandholtz 1992: 92-99, Schneider and Werle, 1990). The mid-1980s saw the beginnings of EC action, leading to a Green Paper in 1987 (CEC 1987). Thereafter, an increasingly rapid flow of regulatory measures (Directives and Decisions) ensued (Thatcher 1997; Sauter 1995, 1997 ch5; Scott and Audéoud 1996). Most concerned competition and comprised two types of provisions. The first were liberalisation measures, in the form of prohibitions on member states from maintaining legal monopolies over supply ('special and exclusive rights'), obliging them to allow competition. Initially, liberalisation was confined to limited segments of the telecommunications market. Thus, for instance, the Terminals Directive of 1988 (CEC 1988) permitted competition in the supply of all types of customer premises equipment. The 1990 Services Directive (CEC 1990) then ended special and exclusive rights over the supply of all telecommunications services, other than 'reserved services' (voice telephony and telex services), whilst the 1994 Satellites Directive (CEC 1994) insisted that competition be permitted in satellite services and equipment and the Mobile Communications Directive (CEC 1996) laid down that competition in mobile services (such as telephony and paging) should be maximised (subject to bandwidth availability) with at least two suppliers being licensed. These segments were growing very rapidly in all four countries from the late 1980s onwards. Nevertheless, the core of telecommunications remained 'network operation'- fixed-line voice telephony and transmission- which accounted for over 85% of telecommunications revenues. However, in the mid-1990s, liberalisation was extended to network operation: in 1995, a Commission Directive allowed cable networks (notably cable television networks) to be used for transmission of all services already opened to competition (CEC 1995); in 1996, a Directive imposed the duty on most member states to allow competition in public fixed-line voice telephony and over the fixed-line infrastructure from 1st January 1998 (CEC 1996).<sup>4</sup> Thus by 1998, the EC regulation banned national monopolies throughout the entire telecommunications sector.

Ending national monopolies was believed to be insufficient to guarantee the development of competition or the ending of traditional patterns of PTO dominance: traditionally, in those limited areas in which competition had been permitted, member

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<sup>4</sup>There were temporary derogations for member states with small or underdeveloped networks; these did not include the four countries studied here.

states had used several instruments to control supply, including the issue of licences, the terms of such licence, refusal of connection to the PTO network and national norms.<sup>5</sup> EC regulation therefore also included a second set of 're-regulatory' requirements, namely a host of rules governing the conditions of supply in order to ensure 'fair and effective' competition. Key conditions of supply for services were laid down in the Open Network Directive (Council 1990), such as non-discrimination, access to networks and cost-oriented tariffs.<sup>6</sup> Others followed that covered issues central to competition throughout the sector: licensing, interconnection and universal service. Thus, for example, the Licensing Directive (EP and Council 1997a) prohibited restrictions on the number of new licences except in specified circumstances (notably to make efficient use of radio frequencies); the licence conditions that national authorities could impose were also limited. A further Directive on interconnection and universal service (EP and Council 1997b) insisted that PTOs should negotiate interconnection with each other on a non-discriminatory basis; PTOs with 'significant market power' were given further duties, such as publication of reference tariffs, cost-oriented tariffs, transparent accounting systems and in some cases, accounting separation. The Directive also defined universal service and specified methods of funding the cost of providing it.<sup>7</sup>

EC measures made no almost mention of ownership, since under Article 222 of the Treaty of Rome, the EC cannot intervene in questions of ownership in member states, nor the structure of suppliers. Nevertheless, EC legislation laid down a few stipulations concerning the institutional position of NRAs ('national regulatory authorities'- ie. those bodies responsible for regulation in member states. The most important was that supply and regulation had to be undertaken by legally separated organisations. However, there was no requirements that NRAs be independent of national governments- indeed, PTT ministries were generally counted as NRAs.

### **III The Impact of EC regulation on liberalisation and the regulation of competition**

Since traditional policy framework in Britain, France, Germany and Italy involved extensive monopolies, EC legislation giving rights to compete and establishing rules for the operation of competition represented a considerable change. Close analysis, however, indicates a complex pattern: EC regulation interacted with other factors operating within the four countries; its impact differed over time; its effects also differed between Britain on the one hand, and the other three countries on the other hand.

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<sup>5</sup>Examples included were specialised forms of CPE and some advanced computer services that used the telecommunications networks; the supply of television sets offered an analogous case.

<sup>6</sup>The ONP Directives was a framework directive that laid down general principles governing the supply of service; it was followed by a series of Directive dealing with specific services such as leased lines and packet switching and voice telephony.

<sup>7</sup> Universal service comprises an 'affordable' voice telephony service via a line that can also support low-speed fax and data services. It can be funded either by a universal service fund at a national level or by supplementary interconnection charges levied by the supplier bearing the 'burden' of universal service.

In the 1980s and early 1990s, EC directives insisting on competition in terminal equipment, and advanced services<sup>8</sup> were largely following reforms rather than leading them: many EC measures had already been introduced or were underway in the four countries. Thus in Britain, BT's monopoly over terminal equipment, 'value-added services' and mobile communications services had been ended in the early 1980s as part of the policy of liberalisation pursued both by the Conservative government and Oftel; competition was extended and new rules were established to ensure that it was 'fair and effective'.<sup>9</sup> Similarly, in France and Germany, PTO monopolies over the supply of customer premises equipment and value-added network services had been restricted during the 1980s, and liberalisation in mobile services began in the late 1980s and early 1990s.<sup>10</sup> In the two countries, EC regulation was an additional factor; it extended the scope of liberalisation and offered refinements to national rules.<sup>11</sup> The EC's greatest impact was on Italy, where the development of competition was slow, EC Directives required implementation and the Commission intervened directly to exert significant pressure for liberalisation;<sup>12</sup> but even so, modest liberalisation was already beginning in the early 1990s as EC legislation was being passed.<sup>13</sup>

The regulatory reforms concerning terminal equipment and advanced services in the four countries were largely driven by non-EC national and transnational factors. One was pressure by large business users who were dependent on high quality advanced telecommunications services and who were dissatisfied with existing PTO supply and restrictions on entry. Thus, for example, large banks and computer companies such as IBM, called for an end to PTO monopolies in advanced services that combined telecommunications and computing and that were vital for their businesses;<sup>14</sup> even in Italy, lobbying for change had been building up from users, notably banks and large industrial companies such as Olivetti and Fiat.<sup>15</sup> Multi-nationals pressed for liberalisation of advanced services and CPE, notably in Germany, where calls for liberalisation were led by IBM, supported by the American government.<sup>16</sup> Excess demand played a central role in the liberalisation of mobile networks in all four countries. Perhaps most important of all, it became increasingly difficult in practice to police and enforce restrictions on CPE and advanced services.

Introducing competition into advanced services and terminal equipment aroused limited controversy: they represented only 10-15% of markets and were not seen as natural monopolies. Much more difficult was network operation- public voice

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<sup>8</sup> CEC 1988, 1990, 1994 and 1996.

<sup>9</sup> Notably over interconnection and cross-subsidisation; see Thatcher, 1994. Armstrong, Cowan and Vickers, 1994.

<sup>10</sup> Schmidt 1991, Thatcher 1999b, Noam 1992.

<sup>11</sup> Thatcher 1995a, 1996; cf. Schneider et al 1994.

<sup>12</sup> Notably over mobile telephony and closed user networks- Il Sole 24 Ore 12.1.95, 20.1.95, 29.3.95, 18.7.95, 4.10.95, 7.6.96 and Stehmann 1995.

<sup>13</sup> For example, in terminal equipment- Foreman-Peck and Manning 1988, Noam 1992.

<sup>14</sup> For Britain, see Financial Times 15.4.80, 24.4.81 and 1.10.82, and Cawson et al. 1990; for weaknesses of German specialised networks, see Jäger 1994.

<sup>15</sup> Richeri 1985, Foreman-Peck and Manning 1988.

<sup>16</sup> Schmidt 1991; Financial Times 31.7.86 and 2.6.86.

telephony and the building and operation of networks- which constituted the core of telecommunications and accounted for over 85% of sectoral revenues. When EC legislation on competition in voice telephony and the operation of networks was passed in 1995-96, the regulatory adaptation required in Britain differed from that of France, Germany and Italy. Britain had already introduced competition into network operation before EC legislation. Hence, the degree of national regulatory modification needed to conform to EC law was very limited. In contrast, France, Germany and Italy still maintained monopolies for their historic PTOs in network operation, and indeed during the 1980s, had made considerable efforts to protect those monopolies.<sup>17</sup> Moreover, the 're-regulatory' elements of EC legislation were largely new: previously there had been few formal requirements over matters such as interconnection, licensing and universal service because of monopoly provision by a state-owned operator.

In these France, Germany and Italy, EC rules had direct and indirect impacts on competition in network operation. In the early/mid- 1990s, liberalisation often met strong opposition, led by trade unions representing PTO employees<sup>18</sup> and parts of the political left.<sup>19</sup> EC requirements provided political impetus to overcome inertia and often active resistance to liberalisation. Thus, for example, legislation in Germany in 1989-90 and 1994 (Postreforms II and III) extending competition was presented as being necessary to meet EC obligations, in the face of powerful lobbying by the DPG trade union; similarly, in Italy, liberalisation in the mid-1990s followed the application of EC law by the Anti-Trust Authority, the requirements of EC law and direct pressure by the EC Commission.<sup>20</sup> Later in the 1990s, in order to comply with EC legal requirements to end remaining monopolies, France, Germany and Italy passed major pieces of legislation,<sup>21</sup> together with secondary legislation. The new laws ended monopolies and laid down rules for the regulation of competition, including matters such as interconnection, universal service and licensing. The role of the EC was enhanced by takeovers and mergers: liberalisation was increasingly made a condition of approval of cross-national cooperation by DG IV, the Competition Directorate of the EC Commission.<sup>22</sup> More generally, EC 'imposed' liberalisation offered an explanation for unpopular developments, such as tariff re-balancing that

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<sup>17</sup> For instance, in France, in the 1980s Cable Plan, the DGT/France Télécom had been careful to prevent use of new cable networks for telecommunications, preventing infrastructure competition- Brenac and Payen 1988; in Germany, Deutsche Telekom owned most of the cable television network.

<sup>18</sup> Such as the CGT and SUD-PTT in France, and DPG in Germany.

<sup>19</sup> Such as the Communist and Socialist parties in France and elements of the Social Democrats in Germany in the late 1980s and early 1990s.

<sup>20</sup> Werle 1999; Natalicchi, 1999; *Il Sole* 24 Ore 6.2.95, 29.3.95, 18.7.95, 7.6.96, 11.9.96.

<sup>21</sup> In France, the 1996 law on liberalisation and competition, no.96-559; in Germany, the 1996 Telekommunikationsgesetz ('Postreform III'); in Italy, the law no. 249 of 31 July 1997; in Britain, minor modifications were required to meet some EC 're-regulatory' requirements- cf. Hunt 1997.

<sup>22</sup> The most prominent example was approval of the France Télécom-Deutsche Telekom joint venture, 'Atlas' in 1995, in which France agreed to allow competition in non-voice services over competing infrastructures earlier than required under EC law- *Les Echos* 10.3.95 and *Le Monde* 22.3.95



favoured businesses rather than most residential users (and voters) by sharply cutting long-distance charges whilst increasing access ones.

However, in the three countries, EC requirements were not the sole factor behind liberalisation; rather, they formed part of reform debates that emerged in the 1990s.<sup>23</sup> Although liberalisation ran counter to traditional PTO monopolies, it was also largely congruent with the strategies or sometimes reluctant expectations, of national governments and PTO managements. The two sets of actors had altered their positions during the 1980s and 1990s, as existing reformist elements within them gained ground. They had gradually accepted during the 1990s that competition in voice telephony and telecommunications infrastructure provision was inevitable and indeed even beneficial. In this change of views, factors other than EC regulation can be identified.

PTO monopolies over voice telephony and the infrastructure appeared to be increasingly difficult or costly to sustain given developing technologies. PTOs faced the development of 'bypass', both directly and indirectly, as other countries liberalised and attracted telecommunications-based firms.<sup>24</sup> There was growing pressure for liberalisation by business users, especially large multi-nationals and particularly when monopoly PTOs could not expand supply sufficiently rapidly. Hence, for example, in Germany, there were strong pressures for liberalisation of infrastructures after reunification, as Telekom could not satisfy demand, whilst in Italy private networks and services were being established (legally or with the tolerance of public authorities) by large companies desperate to obtain a modern telecommunications network.<sup>25</sup> Politically powerful companies which wished to enter the expanding telecoms market also lobbied governments for change.<sup>26</sup>

New ideas about natural monopoly and the benefits of competition spread, as did claims that countries which maintained restrictions would be left behind other countries which had liberalised. At the same time, liberalisation in other nations offered an example, showing that competition was workable and that incumbent PTOs could even thrive in a liberalised market. In addition, overseas policy makers and suppliers argued and lobbied for the end of monopolies. Britain and the United States were particularly important sources of ideas, experiences and arguments for liberalisation. Britain was seen as a dangerous competitor within Europe, thanks to liberalisation, the presence of the privately-owned BT and its policy of attracting large multi-national telecommunications users.<sup>27</sup> Reforms in the United States (notably the ending of AT&T's monopolies and then its break up in 1984) appeared to offer

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<sup>23</sup> For a description of the move towards competition in the 1980s and early 1990s in France and Germany, see Bancel-Charensol 1996; for Germany, see also Werle 1999.

<sup>24</sup> The growth of 'bypass' for lucrative international services brought home the vulnerability of the national PTOs' monopolies- see, for example, the similarity in tariffs on the important North American routes between BT and the DGT/France Télécom- Longuet 1988, p.149.

<sup>25</sup> For telecoms and German reunification, see Robischon 1999; cf. Stehmann 1995, pp.219-221.

<sup>26</sup> For example, CGE in France, Veba and Mannesman in Germany, and Olivetti, Fiat and Mediaset (owned by Silvio Berlusconi) in Italy.

<sup>27</sup> Cf. Dandelot 1993, Larcher 1993, *Il Sole 24 Ore* 6.6.94, 11.5.96, 17.12.96.

opportunities for foreign suppliers, including European ones, to enter the American market,<sup>28</sup> and hence increased the incentives for reciprocal liberalisation in Europe. At the same time, however, it led to direct pressure on European policy makers to open up their markets: after 1984, AT&T pursued a strategy of international expansion, as did the RBOCs in the 1990s.<sup>29</sup> Such companies, together with other such as IBM, lobbied European governments to end PTO monopolies, and were supported by American policy makers.<sup>30</sup> Finally, the success of rapid development of advanced telecommunications/information communications services and networks in Britain and the US was linked to liberalisation of telecommunications, increasing the mimetic pressures on other European countries.

Competition was also intimately linked to privatisation and internationalisation, which were vigorously pursued by France Télécom and Deutsche Telekom with the active involvement of their national governments. Liberalisation was the *quid pro quo* of privatisation, which was strongly desired by PTO managements and governments (see section IV): competition was claimed to prevent private monopoly PTOs exploiting their positions to extract vast profits from users. For the operators, overseas expansion represented a response to increased demand for international services, to alliances being formed by other operators (most notably between BT and the American operator MCI) and to weakening national monopolies.<sup>31</sup> A single European market opened to competition offered greater opportunities for cross-national links, both between them and with other operators. Liberalisation aided internationalisation by justifying alliances with foreign operators by national PTOs, traditionally symbols of national sovereignty. At the same time, it appeared to offer the prospect of prising open the US market, the largest in the world. In particular, the acquisition of shareholdings in US operators and entry to the United States market were made dependent by US regulators and policy makers on ending monopolies in Europe; thus, for example, when France Télécom and Deutsche Telekom sought to take a stake in the American operator Sprint, liberalisation of their home markets was linked to approval by US regulatory authorities.<sup>32</sup>

#### **IV EC regulation and the organisation of the state**

The 1980s and especially the 1990s saw a comprehensive reshaping of state structures in Britain, France, Germany and Italy. In all four countries, changes involved a two-step process away from the traditional structure of the state as regulator, policy maker and supplier. The first stage in reform was that the PTOs (public telecommunications operators) were separated from postal services and made into autonomous publicly-owned companies (or their equivalents), with their own legal identity, leaving the PTT Ministry as the main sectoral regulator. In Britain, British Telecom was created from the Post Office in 1981, the Deutsche Bundespost was divided in 1989-90 into three

<sup>28</sup> Noam 1989, pp.287-290; Dyson and Humphreys 1990.

<sup>29</sup> Ibid, p.281 and Mouline 1996.

<sup>30</sup> Vogel 1996, pp.35-38.

<sup>31</sup> For a discussion of internationalisation and corporate strategies, see Cowhey and Aronson 1993.

<sup>32</sup> La Tribune Desfossés 15.6.94, 4.12.95, Frankfurter Allgemeiner 24.4.95; Wirtschaftswoche 4.5.95.

corporations, including Telekom was separated from for telecommunications and France Télécom became an *exploitant public* in 1990. The reform process in Italy involved the largest supplier, ASST, being removed from the PTT Ministry in 1992<sup>33</sup> and then consolidation in 1994-96, through the creation of Telecom Italia, which brought together all the various publicly-owned operators.

Thereafter, the PTOs were wholly or partially privatised. Hence 50.1% of shares were sold in BT in 1984, with the remainder being disposed of by 1993. A minority of shares in Deutsche Telekom (DT) and France Télécom were sold in 1996-98, whilst a majority of Telecom Italia shares were sold in 1997. New regulatory authorities were created that were semi-independent from elected politicians: Oftel (the Office of Telecommunications), the ART (Autorité de régulation des télécommunications), the Regulierungsbehörde and the Autorità for Telecommunications and Broadcasting. They enjoyed considerable formal powers over enforcing licences and ensuring that competition was 'fair', leaving governments with more general functions, notably over licensing and defining the framework of competition.

EC legislation contained few requirements concerning the organisation of the state. Even the most important stipulation in Directives -that supply and regulation were to be undertaken by separate organisations- prohibited PTOs from continuing to act as regulators, but did not necessitate PTOs ceasing to be part of the civil service. Other changes, such as privatisation and independent regulators, were not part of EC legislation. Thus the reforms did not represent the transposition of EC legal measures into national law.

Nevertheless, in France, Germany and Italy, the EC played an important role in the reform process in the late 1980s and the 1990s by altering national reform debates and increasing pressures for change. Its regulatory regime, centred on 'fair and effective competition', undermined traditional justifications for public sector supply, such as 'service public', cross-subsidisation and support for domestic manufacturers. It increased pressures on governments and PTOs to alter existing structures: liberalisation engendered processes of entry that appeared to disadvantage suppliers who failed to alter their organisational forms and that increased incentives for governments to distance themselves from supply. The EC weakened opponents of institutional modifications and providing arguments for reformers.

PTO managements in France, Germany and Italy argued that EC liberalisation made reform urgent and indispensable. They claimed that they needed to adjust to a competitive market and that public sector ownership, especially within the civil service, inhibited them from competing effectively, because they faced constraints concerning staffing, contracts and expenditure.<sup>34</sup> The entry of powerful, expansionist operators such as BT and AT&T, advantaged by private ownership, experience of competition and international alliances was invoked, especially in France and Italy.<sup>35</sup> Brandishing the date of 1 January 1998 (the EC deadline for full competition), PTO

<sup>33</sup> It became part of the publicly-owned IRI group.

<sup>34</sup> Roulet, 1994, *Le Monde*, 6.7.93, 16.7.93; Chevallier, 1996, Schmidt 1996b; *Il Sole 24 Ore* 5.8.95, 11.5.96, 6.6.96, 15.2.97.

<sup>35</sup> See, for example, Larcher 1996, *Le Monde* 7.6.97, *Il Sole 24 Ore* 6.6.94, 29.6.95, 11.5.96.

managements pressed hard for reforms, lobbying governments and mounting public campaigns. Thus, for example, the head of France Télécom linked acceptance of a new law implementing EC competition provisions to the passage of another bill to alter France Télécom's organisational position; the issue became so heated that his replacement resigned after only ten days in 1995, due to a failure to receive sufficient assurances from the government that liberalisation of network operation would be accompanied by organisational changes for France Télécom.<sup>36</sup> Similar pressures, utilising the 'threat' posed by full competition were exerted in Germany by Deutsche Telekom and also by reformers in Italy.<sup>37</sup>

EC regulation also contributed to decisions by governments in France, Germany and Italy to introduce reforms despite opposition and controversy. On the one hand, the EC could be used to justify reforms. Thus, for example, EC requirements prohibiting PTOs from continuing their regulatory functions formed part of arguments by PTO managements and governments in France and Germany for removing PTOs from the civil service structures and making them legally separate bodies from PTT Ministries.<sup>38</sup> On the other hand, governments faced pressures for change not only from their national champion PTOs, but also from competitors to PTOs, who, armed with EC rights, took action to obtain 'fair' treatment. As a result, continued direct regulation of telecommunications became a legally and politically contentious area. Governments faced sharp conflicts between protecting their PTOs and their legal obligations under EC law concerning competition. Telecommunications regulation thus began to offer potentially damaging controversies. The clearest cases arose in Italy, where governments found themselves embroiled in lengthy disputes, caught between Telecom Italia, the Italian Anti-Trust Authority, the EU Commission (particular its powerful competition Directorate, DG IV) and large, influential new entrants such as Olivetti and Fiat.<sup>39</sup> In addition, IRI, the state umbrella company that owned certain operators was so overburdened by debt that, faced with European state aid law, reorganisation was agreed between the Italian government and the competition Directorate General (DG IV) of the Commission.<sup>40</sup> Moreover, implementing EC law involved highly technical decisions over matters such as such as interconnection charges, apportionment of costs and estimates of losses for universal service provision. The EC regulatory framework therefore increased the incentives for governments to cease combining the roles of policy makers, regulators and suppliers.

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<sup>36</sup> Le Monde 10-11.9.95.

<sup>37</sup> Die Zeit 4.12.92, Financial Times 11.3.93, 26.10.93; Il Sole 24 Ore 29.6.95, 6.12.96, 15.2.97 and 17.3.97.

<sup>38</sup> Cf. Prévot 1989, pp.133-136, Le Monde 13.10.90 and 6.7.93; Schmidt, 1991.

<sup>39</sup> One example was the payment of 750 billion lire demanded of Omnitel for its advanced (GSM) mobile telephony licence, which led to infringement proceedings by the Commission and repayment of monies-; another was the opening of closed user group networks- see Corn et al 1995.

<sup>40</sup> In the agreement in 1993 between competition Commission Van Miert and the then Foreign Minister, Beniamino Andreatta, the Commission promised not to take legal action concerning state aids if IRI's debts were reduced, which Italy stated would be achieved through some form of privatisation of Telecom Italia.

National coalitions supporting traditional state structures found themselves placed in a defensive position by the EC regulatory regime and struggling against a gradual set of changes that undermined their position and cohesion. Their core members were PTO trade unions and employees, who wished to protect the status of employees, and nationalistic supporters of public ownership (traditionally present in parties of both the political left and right) who argued that states should conserve vital areas of economic life under their direct control and prevent private monopolies from exploiting users.<sup>41</sup> However, in the face of EC liberalisation, the nationalist wing of the coalition shrank, as the previous reasons for its support for state ownership of PTOs were gradually removed: competition and regulation rendered public ownership unnecessary to prevent monopoly exploitation of users by private suppliers; reforms were needed for national champion PTOs to survive and prosper. Moreover, EC 'imposed' competition offered a convenient argument for governments of the left faced with opposition from within their parties and coalitions.<sup>42</sup> Thus in France, Germany and Italy, political parties that had hitherto opposed reforms, supported and often introduced them.<sup>43</sup> Trade unions and employees were left isolated, appearing to cling to outdated structures in pursuit of narrow sectional interests, in the face of EC regulation based on competitive markets and successful examples of privatisation that threatened to leave unreformed 'national champion' PTOs vulnerable.

Nevertheless, whilst EC regulation aided reformers and increased incentives for institutional modifications, it was an influence additional to other factors: its role in national politics was to accelerate and facilitate strategies driven by non-EC developments. The process of reform had begun at the national level during the 1980s, as PTO managements and national governments sought to adapt to new conditions. Britain represented an extreme case: organisational reforms (notably the privatisation of BT and the establishment of OfTel, the semi-independent regulator) were introduced in 1984 and without reference to the EC. In France and Germany, attempts to move away from civil service status for PTOs were long-standing, dating from the 1960s and 1970s. Then in the mid/late 1980s, the reform movement was revived in earnest, just as the EC began to develop its regulatory framework. Thus in France, in 1988 the Rocard government established a special commission to examine alteration of France Télécom's organisational position,<sup>44</sup> which led to legislation in 1990 that transformed the operator into an exploitant public.<sup>45</sup> In Germany, the process of reform also got underway through the Witte Commission which was established in 1985 and proposed in 1987 that the Deutsches Bundespost be split into three public

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<sup>41</sup> Werle 1999; Foreman-Peck and Manning 1988; Richeri 1985; Cohen 1992; Thatcher 1999b.

<sup>42</sup> Indeed, in Italy the Commission intervened directly as the privatisation of Telecom Italia was linked to the 1993 agreement on state aids; thus the Commissioner for competition, Karel Van Miert, discussed privatisation with Italian policy makers in 1995-96- *Il Sole* 24 Ore 3.3.95, 7.6.96, 11.9.96.

<sup>43</sup> The most striking examples were in France and Italy, where governments of the left depended on support from Communist or former Communist parties: in the former, partial privatisation of France Télécom after June 1997 also ran counter to the election promises of the PS; in Germany, the Social Democrats also accepted reforms, citing EC competition as a major reason- *La Tribune* Desfossés 17.5.93.

<sup>44</sup> Prévot 1989.

<sup>45</sup> Thatcher 1995b, Gensollen 1991.

corporations, one being Telekom.<sup>46</sup> In Italy, there had been extensive discussion of reorganisation, although little action was taken because weak governments failed to overcome opposition from political parties and trade unions.<sup>47</sup>

The process of institutional modification accelerated during the 1990s in France, Germany and Italy, due to both EC regulation and non-EC factors. Rather than representing a decisive break or central pressure for change, the EC regulatory regime largely represented a factor congruent with other forces, as reforms were selected and supported by PTO managements and governments for non-EC reasons.<sup>48</sup>

Financial constraints that were unrelated or only partially related to the EC's regulatory regime in telecommunications were central in reforms. For governments, privatisation offered vital fiscal advantages, as sale receipts allowed governments to reduce debt and meet the Maastricht criteria for public debt; in addition, in Germany and Italy, it avoided use of public funds for essential investment. For their part, PTO managements had become increasingly resentful during the 1980s and 1990s at their continuing use as instruments of fiscal and industrial policy- for instance, providing payments to the general budget, covering the losses of postal services and offering secure employment.<sup>49</sup> They therefore pressed hard for a new settlement that would free them of such burdens; having achieved legal autonomy as public corporations, they lobbied for privatisation in the 1990s.

The changing demands of telecommunications markets offered another set of pressures for structural reform. PTOs sought restructuring to escape the constraints of the public sector and to adapt to competition; irrespective of EC regulation, their monopolies were being reduced as the fastest-growing services (such as mobile telephony and advanced services mixing telecommunications and computing) had already been opened to competition. Thus, for example, one of the experiences that impelled Deutsche Telekom to press for privatisation was competition in mobile telephony: following a German government decision to license a second operator (Mannesmann), it found itself outclassed by the newcomer. Large-scale investment was needed to support advanced services and meet new entrants. Capital requirements were particularly important in Germany, where, following reunification, the costs of modernisation in the former East Germany were very large<sup>50</sup> and the German Monopolies Commission suggested allowing competition;<sup>51</sup> privatisation offered the prospect of easier access to capital markets and substitution of equity for debt and hence protection of Telekom's dominant position. In Italy, reform was useful because the network needed heavy investment for modernisation.

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<sup>46</sup> Regierungskommission Fernmeldewesen 1987; for a history, see Werle 1990.

<sup>47</sup> See Foreman-Peck and Manning 1988; Richeri 1985.

<sup>48</sup> For a general discussion of factors responsible for privatisation and changing state structures in Western Europe, see Wright 1994.

<sup>49</sup> See Cohen 1992, Thatcher 1999b, Koebberling 1993, pp.55-57; for Italy, comments by Francesco Chirichigno (administratore delegato of Telecom Italia), *Il Sole 24 Ore* 25.6.95; personal interviews.

<sup>50</sup> An estimated DM60 billion was required between 1990 and 1997; by 1992, Telekom faced debts of DM100 billion, and debt servicing costs represented 12% of its income of DM 54 billion- *The Economist* 30.10.93.

<sup>51</sup> See Koebberling, p.61.

Internationalisation was often a key justification for privatisation. PTOs in France, Germany and Italy wished to internationalise, in order to enter the American market and to offer 'global networks and services', especially to multinationals<sup>52</sup> and to match rival PTOs throughout the world, who were forming alliances.<sup>53</sup> Governments wished to protect and promote their own 'national champion' PTOs, and hence supported changes that aided PTO internationalisation and business success. However, forming international alliances appeared to require privatisation; public ownership prevented cross-share holdings, made it difficult to value the operators and appeared to render decisions vulnerable to 'political influence'.<sup>54</sup> At times, internationalisation involved very direct linkages to institutional change. Thus, in forming the alliance between France Télécom and Deutsche Telekom, German policy makers called for privatisation of the former.<sup>55</sup> In the battle between BT and France Télécom to link with the American operator MCI in 1993, MCI chose the former; the head of France Télécom claimed that public ownership had been an important obstacle to success.<sup>56</sup> Similarly, obtaining regulatory approval by US authorities for an alliance by the two operators with the American operator Sprint became enmeshed in France Télécom's privatisation.<sup>57</sup>

Ideas about how 'public interests' should be protected also altered in the four countries. Telecommunications formed part of the international wave of attacks on state ownership in the 1980s and 1990s.<sup>58</sup> Cross-national policy learning and emulation were important in France, Germany and Italy: the privatisation of BT and the establishment of Oftel in Britain were used as examples of change.<sup>59</sup> Governments saw increasing disadvantages in existing structures and set of relationships as they faced conflicting claims and interests. In particular, the historic PTOs pressed for protection from increased competition and when dissatisfied, openly dissented,<sup>60</sup> whilst at the same time, new entrants (who often included powerful private firms) lobbied for favourable terms and restrictions on the historic PTO.<sup>61</sup> In addition, the

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<sup>52</sup> See, for example, comments by Ron Sommer, head of Telekom- Die Welt 6.2.96, and for Italy, Il Sole 24 Ore 29.6.95, 5.8.95, 11.5.96, 12.96, 15.2.97.

<sup>53</sup> Elixmann and Herman 1996; Cowhey and Aronson, 1993, pp.191-6.

<sup>54</sup> See Roulet 1994, Dandelot 1994, Senate reports by Gérard Larcher 1993 and 1996.

<sup>55</sup> See the comments by Gunter Rexrodt, German Finance Minister- La Tribune Desfossés 18.7.5 and Le Monde 22.7.95.

<sup>56</sup> Le Monde 6.7.93

<sup>57</sup> (Le Monde 3.8.94, 22.7.95)

<sup>58</sup> Cf. Henig and Hamnett 1998; Ikenberry 1990; Wright 1994.

<sup>59</sup> At times, copying was explicit- for example, in France, the DGPT/DRT made explicit references to Oftel- see its Rapports d'Activité; similarly, one of the justifications for establishing an independent regulator in Germany was the example of Oftel- Die Welt 26.8.95; in Italy, Romani Prodi (Prime Minister 1996-98 and former head of IRI) had also looked to the British example- see Il Sole 24 Ore 10.11.95.

<sup>60</sup> France Télécom openly led a campaign for change after 1993; Deutsche Telekom threatened to establish further private subsidiaries in the mid-1990s- Frankfurter Allgemeiner 15.11.94.

<sup>61</sup> For example, the Compagnie Générale des Eaux in France, Veba and Mannesmann in Germany and Olivetti in Italy.

increasingly important and demanding large users needed to be satisfied, notably through tariff rebalancing, to increase access and local call charges and reduce long-distance tariffs, a move that threatened to be unpopular with voters who, as domestic consumers, often lost out. Existing regulators within governments and general competition authorities pressed for a reduction in 'political interference' and structures that supported 'fair competition and did not favour incumbent PTOs'.<sup>62</sup> Given these developments, privatisation and a more distant relation between governments and suppliers, mediated by a semi-independent regulator, allowed elected politicians to avoid or deflect pressures that were increasingly difficult to manage successfully.

## V Conclusion

In France, Germany and Italy, EC regulation aided institutional reforms. It did so both through its legal requirements and more indirectly, through the repercussions of liberalisation for existing organisational arrangements, thereby extending its influence well beyond its formal legal requirements. It strengthened the position of reformers in the three countries: it offered them additional arguments to justify changes; their coalitions were broadened as EC decisions contributed to the alteration of the preferences and strategies of PTO managements, governments, political parties and officials in the domestic policy process. On the other hand, EC regulation weakened the position of opponents of new forms of supply and regulation. Their previous coalitions were reduced, as nationalistic supporters and political parties abandoned them. Trade unions and employees found themselves isolated and confronted by the logic of the EC's regulatory regime which conflicted with their aims and afforded them few arguments in debates on preserving monopolies and civil service supply of telecommunications services.

Although EC measures constituted a pressure for change, they also formed part of broader processes of telecommunications reform at the national level. Attempts at reorganising telecommunications had begun in the 1960s and by the 1980s, when EC regulation began, a number of certain alterations had already been implemented by member states; in these respects, EC legislation was following behind domestic action. The most pronounced example was Britain, where EC decisions required almost no domestic alterations; however, in the other three countries, most early EC requirements had also been introduced. Later EC decisions did require considerable institutional modifications in France, Germany and Italy. Nevertheless, the expansion of EC activities was in fact closely intertwined with the dynamics of domestic reform in the three countries. Change had begun, as PTO managements and governments modified their strategies in response to non-EC factors and began to support or accept liberalisation and reorganisation of supply during the 1980s. However, they were

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<sup>62</sup> Thus, for example, in France, Bruno Lasserre, the head of the DGPT (Direction générale des postes et télécommunications), the regulatory unit in the PTT Ministry in France), was central in drafting the 1996 law setting up the Autorité de Régulation des Télécommunications; in Italy, the head of the Anti-Trust Authority, Giuliano Amato, led pressures for the formation of the Autorità, both through direct intervention and because of his activism in applying competition law to telecommunications- personal interviews; DGPT 1994, *Il Sole 24 Ore* 22.11.95, Natalicchi 1999.



confronted with a powerful domestic coalition that blocked rapid reform. During the 1990s, their preferences and strategies continued to evolve, in part because of EC measures but in large measure because of other factors. At the same time, they were able to use the EC's regulatory regime to justify further reforms in pursuit of their strategies of adaptation to changing domestic and international conditions in telecommunications, whilst seeing domestic opponents weakened.

National modifications were therefore driven by a host of factors, of which the EC was only one. Indeed, closer inspection of domestic politics indicates the importance of non-EC influences in the shifting strategies of key actors. In particular, PTO managements and governments increasingly favoured liberalisation and reorganisation of PTOs in order to adapt to changing conditions, including technological and economic developments, frustration by PTO managements with their position within the public sector, increasing conflicts for national governments between their roles as regulators and owners of suppliers, pressure by users and new entrants and the desire for PTOs to internationalise.

Conclusions from telecommunications can be used to address broader issues about the impacts of Europe, especially on institutional reform. EC regulation contributed to modification of formal institutional arrangements, both by enhancing existing desires for change and by providing an additional argument for reformers to justify and accelerate change. In France, Germany and Italy, several major institutional alterations were introduced in the late 1980s and 1990s; moreover, the new arrangements greatly differed from the traditional ones that had lasted for decades, often dating back from the beginning of telecommunications. The impacts of EC regulation help to counter claims of great national institutional stability (Hall 1986; Immergut 1992; Weir 1992; Hattam 1993; Steinmo 1993; Dobbin 1994). They represent an explanatory factor for change and also challenge arguments that national institutions change very rarely, in times of crisis (Thelen and Steinmo 1992; Krasner 1984). In addition, telecommunications suggests that certain types of actor in the institutional reform process were advantaged (PTO managements and governments), as they were able to utilise EC regulation for their strategies, whilst others were disadvantaged (notably trade unions). The 'two-level game' (cf Putnam 1988, Evans et al 1993) or 'multi-level governance' (cf. Marks 1993, 1997, Hooghe 1996, Marks et al 1996) of EC regulation was therefore not neutral, but contributed to altering the distribution of power at the domestic level.

The importance of EC regulation grew over time: in the late 1980s and early 1990s, EC decisions largely followed existing national ones or processes of change already underway in member states. By the mid-1990s, EC actions concerned the core of the telecommunications sector and required considerable institutional alterations in France, Germany and Italy. Appreciation of the role of the EC, however, must extend further than its legal requirements: the 1990s saw crucial indirect effects, as the logic of EC rules undermined existing arrangements and provided arguments for reformers for changes that went far beyond EC legislation, notably privatisation. Telecommunications thus suggests that the role of Europe has spread and its forms are varied, with many of its most significant impacts arising from the repercussions of initially relatively limited decisions.

Telecommunications also shows that analysis of the role of EC regulation requires an understanding of its interaction with other forces for change operating within member states (cf Héritier, Knill and Mingers 1996). Impacts varied among countries, depending on their existing institutional position; hence not only is EC regulation a 'patchwork' (Héritier 1996), but so are its impacts. Moreover, EC decisions were used by actors at the national level to pursue strategies that were in large measure responses to non-EC factors- technological and economic pressures, new ideas and changing international conditions. The role of the EC's regulatory regime was therefore to reinforce and accelerate moves towards liberalisation and public sector restructuring and to assist reformers in PTOs and national governments in pursuing their strategies of adaptation to new conditions. The force of EC regulation lay in its compatibility with these other factors. However, it also meant that it was one factor amongst several responsible for institutional reform. Hence, EC regulation must be considered in its context, both national and international: although for analytical purposes it may be useful to separate it out, it is not an isolated influence but forms part of complex processes of change driven by factors operating at national and international levels.

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