

COMMISSION

COMMISSION DECISION

of 27 July 1994

relating to a proceeding pursuant to Article 85 of the EC Treaty and Article 53 of the EEA Agreement

(Case IV/34.857 — BT-MCI)

(Only the English text is authentic)

(Text with EEA relevance)

(94/579/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Whereas :

Having regard to the Treaty establishing the European Community,

Having regard to the Agreement on the European Economic Area,

Having regard to Council Regulation No 17 of 6 February 1962, First Regulation implementing Articles 85 and 86 of the Treaty⁽¹⁾, as last amended by the Act of Accession of Spain and Portugal, and in particular Articles 2, 6, and 8 thereof,

Having regard to the application for negative clearance and the notification for exemption submitted, pursuant to Articles 2 and 4 of Regulation 17, as converted on 18 September 1993 from the original notification pursuant to Council Regulation (EEC) No 4064/89 of 21 December 1989 on the control of concentrations between undertakings⁽²⁾,

Having regard to the request made by the parties on 10 February 1994, to extend the application and notification to Article 53 of the Agreement on the European Economic Area,

Having regard to the summary of the application and notification published pursuant to Article 19 (3) of Regulation 17 and to Article 3 of Protocol 21 of the EEA Agreement⁽³⁾,

After consultation with the Advisory Committee for Restrictive Practices and Dominant Positions,

I. THE FACTS

A. INTRODUCTION

- (1) The present case was originally notified as a concentration pursuant to Regulation (EEC) No 4064/89. However, the Commission concluded that none of the transactions notified constituted a concentration. The parties were so informed by the decision of 13 September 1993. Consequently, and at the request of the parties, the notification was converted into a notification for negative clearance and/or exemption pursuant to Regulation 17.

Following the entering into force of the Agreement on the European Economic Area (EEA Agreement), the parties requested the Commission to extend the notification to cover also Article 53 of the EEA Agreement. Given that the notified agreements will have a relevant impact on the EFTA countries and that such impact is expected to be very similar to that the notified agreements will have on the Community, the Commission will also apply Article 53 of the EEA Agreement in the present case.

- (2) The notified operation actually comprises two main transactions :
- (i) British Telecommunications plc (BT) is to take a 20 % stake in MCI Communications Corporation (MCI), worth US\$ 4,3 billion. BT will acquire new equity and will become the largest single shareholder in MCI, with proportionate

⁽¹⁾ OJ No 13, 21. 2. 1962, p. 204/62.

⁽²⁾ OJ No L 395, 30. 12. 1989, p. 1 (corrected version OJ No L 257, 21. 9. 1990, p. 13).

⁽³⁾ OJ No C 93, 30. 3. 1994, p. 3.

board representation and investor protection. As will be further detailed later, several provisions have been included in the relevant agreement to impede BT from controlling or influencing MCI;

- (ii) the creation of a joint-venture company, Newco, for the provision of enhanced and value-added global telecommunications services to multinational (or large regional) companies. The parties will contribute their existing non-correspondent international network facilities, including Syncordia, BT's existing outsourcing business, to Newco.

In the framework of the operation, the parties will rationalize their respective holdings in other telecommunications operators (TOs) and groupings in the world. In this respect, MCI has already acquired most of BT's existing business in North America.

B. THE PARTIES

- (3) BT, the former UK monopolist telecommunications operator, and now a publicly quoted company, supplies telephone exchange lines to homes and businesses; local, trunk and international (to and from the United Kingdom) telephone calls; other telecommunications services and telecommunications equipment for customers' premises.

Worldwide turnover for BT in 1993 was ECU 17 952 million, a figure that shows a slight decrease in respect of 1992 (ECU 18 080 million). Over 95 % of BT's turnover was obtained in the EEA, mainly (over 94 %) in the United Kingdom. Outside the United Kingdom, BT has an established presence in France, the Netherlands, Germany and Spain, where it has recently announced a joint-venture agreement with Banco de Santander to provide data transmission services in Spain, where it has recently announced a joint-venture agreement with Banco de Santander to provide data transmission services in Spain in competition with the local TO.

BT is the world's fourth largest telecommunications company in terms of traffic (minutes of telecom traffic).

- (4) MCI is a telecommunications common carrier in the United States of America providing a broad range of US and international voice and data communications services including long-distance telephone, record communications and electronic mail services to and from the US.

Worldwide turnover for MCI in 1992 was ECU 8 137 million. MCI's turnover in the Community

for the same year was said by MCI to be ECU 326,27 million.

MCI is the second largest long-distance operator in the United States of America after AT&T and the world's fifth largest in terms of traffic.

C. THE RELEVANT MARKET

1. Newco

- (5) The market Newco will address is the emerging market for value-added and enhanced services to large multinational corporations, extended enterprises and other intensive users of telecommunications services provided over international intelligent networks. This market will cover a wide range of existing global trans-border services, including virtual network services, high-speed data services and outsourced global telecommunications solutions specially designed for individual customer requirements. Initially, however Newco will focus its development efforts on the biggest [...] (!) multinationals.
- (6) In this market, Newco is expected to offer a portfolio of global products included in six categories of service offerings. Those global products will originally be based on a blend of existing products of the parent companies.

The six categories are the following:

- data services: low-speed packet, high-speed packet and frame relay services, pre-provisioned, managed and circuit switched bandwidth,
- value-added application services: value-added messaging and video conferencing services,
- traveller services: global calling card services,
- intelligent network services,
- other services: Integrated VSAT network services,
- global outsourcing that will allow the distributor to offer its customers the ability to transfer responsibility and ownership of their global networks to either the distributor or Newco. In this respect, Newco will be able to integrate within its own offerings third-party products already owned by customers that they want to keep.

(!) Blanks between square brackets indicate business secrets deleted pursuant to Article 21 (2) of Regulation No 17.

Given the needs of big companies to link locations geographically dispersed over the world (that means also providing broad coverage of delivery capacity and in-country support), those products must be global in nature and respond to a very particular set of requirements.

For a product to be global, it must have a number of special characteristics that make it different from similar products. Those characteristics are :

- to provide ubiquitous service across multiple borders,
- to provide consistent service levels and flexible delivery schedules,
- to make time-zones, languages and currencies irrelevant,
- to overcome inadequacies of local infrastructures,
- to make customers assume service is local when it is actually being provided from the other side of the world.

(7) The requirements of big companies that a provider of services must meet, and that refer to all products or services being provided are :

- a single point of contact accountable for assuring service levels,
- seamless, uniform, flexible features/functionality across geography,
- end-to-end provisioning, installation, fault management and service support,
- reliable service,
- customized billing, management information, reporting with language and currency flexibility,
- speed, ease of implementation,
- products that meet existing and evolving needs.

Generally speaking, those requirements have not been adequately satisfied under the still existing structure of the global telecommunications market based on national monopolies. A national TO does not provide real one-stop-shop, end-to-end or seamless services to customers' premises located outside the national borders. What a TO was doing up to now was to cooperate with other TOs to link their respective networks. Doing so meant that customers were billed separately and in different currencies by the TO of each country where they had facilities, that services and features available in each country were different (or at least that some features available at home were not available

abroad), and that they had to face many other problems linked to the differences in culture or language.

(8) This situation began to change because of two elements. The starting up, first in the United States of America, then in the United Kingdom and now in the rest of the Community, of the gradual liberalization process of the global telecommunications market, and, secondly the rapid convergence of telecommunications and information technology. Both elements enabled the introduction of new services and products which vastly improved quality and range. One result was that multinationals and other big companies began to construct their own private networks. However, those private networks were costly because they eliminated scale economies of service and personnel, and because telecommunications was not the core business of those companies. For those reasons, now that the continued evolution of the said two elements has substantially changed the overall situation, those companies may consider turning to telecommunication service providers such as Newco.

(9) In addition, as regulation eases and technology advances, the border between services still under monopoly and liberalized services fades away. This fact adds further uncertainty to the market.

(10) In this context, what BT and MCI intend to offer through Newco is what the existing technology allows them to offer within the current regulatory limits. New products within existing categories and new categories of products could be offered by Newco in the years to come, that could include public basic telecommunications services.

(11) However, this Decision relates only to Newco's range of products and business scope as notified. Any substantial change thereof in the years to come, and in particular the offering by Newco of public basic telecommunications services will then require a new notification.

Structure of the market

(12) It is particularly difficult to give a precise picture of the existing structure of this emerging market because its principal feature is that it is in constant evolution. What is certain is that there is a very significant growth potential in the segment to be addressed by Newco, due to the continuing emergence of new technologies, improvements in basic infrastructure, the increasing standardization of services across borders, the increasing sophistication of customers and their reliance on telecommu-

nications as a transport vehicle for information. All this is in the framework of a rapidly changing telecommunications regulatory environment, which, in the Community, will mean full liberalization telephony in 1998 (2003 for some Member States).

2. BT's investment in MCI

- (13) The acquisition by BT of new equity equivalent to a 20 % stake in MCI is intended to serve a common interest expressed by the parties to go global to better serve (and keep) their existing customers and to better address new areas of the market.
- (14) The telecommunications market is developing fast and there is a high degree of uncertainty about how it will look in a few years' time: the prospect of full liberalization is pushing TOs to take positions, in order to be in the best possible situation when full liberalization comes. Many alliances are being announced, and most of them include provisions to enter the value-added segment, as a first step (in the EEA, value-added and enhanced services have already been liberalized), in particular as regards the provision of advanced value-added services to big multinationals. In this respect, the creation of Newco and the investment of BT in MCI are steps taken by the two parent companies to pre-position themselves for when full liberalization is in place, steps that are being followed by many TOs who are creating sets of products comparable to those of Newco.

3. Geographic scope

- (15) The geographic market to be addressed by Newco, and to be considered in respect of the investment of BT in MCI, is global. Such conclusion is based on the two following arguments.

Although national borders are still in place as regards the provisions of most telecommunications services, strategic alliances like the present one are being created now in anticipation of a market situation where national boundaries will have substantially disappeared.

In addition, both the services that Newco is going to offer, as indicated in definition of the business scope of Newco (see recital 23), and the customers it intends to serve are by nature international;

consequently Newco will not be involved in the provision of services within one country only.

4. Market shares of Newco

- (16) Newco's addressable market has been estimated by the parent companies at ECU [...] billion in 1994 and is projected to achieve over [...] annual growth over its first five years to achieve ECU [...] billion in 1999. It is also estimated that the Community will account for [...] of the market in 1994/95 rising to [...] in 1998/99.

According to Newco's business plan its market share, considering all categories of services together, will be [...] in 1994 and grow to over [...] by 1999 (assuming no dramatic change in the categories of products offered).

5. Main competitors of Newco

- (17) Many companies, on their own or in cooperation with other partners, have entered or are entering the market for international value-added services (the precise set of services being offered is never exactly the same). Among them, the most important are: AT&T Worldsource, AT&T Istel, GEIS, International Private Satellite Partners (limited to North America and Europe), Eunetcom, Unisource, Infonet, Sprint International, FNA (limited to financial services), and IBM (through IBM's connect programme). Some of those projects are the current expression of strategic alliances between TOs, the real scope of which is not well determined yet, but which are similar to the present one between BT and MCI in that they are actions intended to position their partners with a view to the full liberalization to come and are not limited to the provision of value-added services.

In addition, almost every TO in Europe and in North America is trying to offer to its existing customers, at a national or a limited international level, an improved set of value-added and enhanced services.

For many of them, the range of specific products they want to offer and the kind of customers they want to serve are not clear yet. However, a substantial number intends to address the needs of the same companies Newco sees as potential customers, so that it is anticipated that there is going to be substantial competition at least at that level.

It should also be noted that a substantial number of major companies whose needs Newco intends to address have installed or are in the process of installing their own internal networks built on circuits leased from TOs. Those networks will be close substitutes of the Newco's services, in so far as they are to be offered to third parties.

6. Position of buyers

- (18) The customers that Newco intends to serve are multinational corporations, extended enterprises, and other intensive users of telecommunications and in particular the biggest [...] of them. Many of them have huge telecommunication needs. In addition many have developed experience in the management of their own internal networks. They will only switch to providers such as Newco, if so doing proves to be cost-effective. Finally, given their knowledge of the market they are in a position to request offers from different competitors. All those factors give them considerable bargaining power which will give rise to pressure on margins and an expected high level of competition between suppliers.

D. THE TRANSACTION: THE NOTIFIED AGREEMENTS

- (19) The complexity of the operation concluded between BT and MCI is reflected by the substantial number of agreements notified to the Commission. Those agreements are summarized below:

1. Agreements regarding Newco

(i) *The joint-venture agreement (JVA)*

This is the principal document creating Newco. Under it, the parent companies indicate their intention to achieve joint success in the global telecommunications market and to offer a seamless set of global enhanced and value-added products to the customers of MCI and BT.

- (ii) *The intellectual property agreement (IPA)* concluded by BT, MCI and Newco concerning

the licensing to Newco of the parent companies' technical information and intellectual property rights needed by Newco to carry out the business, and the licensing of Newco's technical information to the parent companies.

- (iii) *The BT/MCI services agreements (SA)*, under which Newco and each parent company (acting as supplier) agree on the terms and conditions of supply of support services to be provided by each parent company to Newco, related to the establishment by Newco of the global platform and on the provision by Newco of the global products and services.
- (iv) *The BT/MCI distribution agreements (DA)* under which Newco appoints each parent company (acting as distributor) as its exclusive distributor for global products in the Americas, in the case of MCI, and in the rest of the world, in the case of BT.
- (v) *The agreement for the sale and purchase of the business of Syncordia (with a disclosure letter)* concluded between Newco and BT setting the terms and conditions of the sale of the assets and business included in Syncordia, which up to now was BT's outsourcing unit.
- (vi) *The Infonet indemnity agreement* concluded between BT and MCI under which MCI undertakes to indemnify and hold BT harmless from and against any legal action by Infonet against MCI, arising from MCI's ownership in Infonet.

2. Agreements regarding BT's investment in MCI

- (20) (i) *The investment agreement (IA)* under which BT has agreed to purchase 20 % of the outstanding shares of common stock of MCI.
- (ii) *The registration rights agreement* concluded between BT and MCI, required in order for each party to effect the transactions contemplated by the IA.
- (iii) *The McCaw indemnity agreement* under which BT undertakes or indemnify MCI and hold it harmless in respect of any legal action by the cellular phone company McCaw against BT as owner of a number of shares in McCaw.

- (iv) Finally, the transaction also includes three agreements relating to the sale by BT to MCI of most of its existing activities in the United States of America and Canada.

3. Contractual provisions

- (21) Relevant provisions of the agreements from a competition point of view are further detailed below.

A. Concerning Newco

(i) Structure of Newco

- (22) Newco is an international joint-venture company, and according to the parties, the central focus of their alliance. Following the incorporation of Newco, 75,1 % of its share capital will be owned by BT and 24,9 % by MCI. Each party will have the right to appoint Newco board directors in accordance with its shareholding. Thus BT will be entitled to nominate six out of eight directors (the A directors) and MCI two out of eight (the B directors).

Most decisions of the board are to be adopted by simple majority of the directors present at any board meeting. However, a number of important decisions cannot be adopted without the prior consent of both shareholders. Most important of those decisions are changes in business direction, management appointments (including the appointment of the chief executive officer) and approval of the five-year business plan and annual operating plan and budget, so that MCI has joint control of the company (this was the conclusion of the Commission in its decision of 13 September 1993).

The day-to-day management and operations of Newco will be delegated to a chief executive officer who will be responsible to the board for all matters in the ordinary course of business.

Newco will be incorporated in the United Kingdom with day-to-day management vested in a US-based service company. It is expected to employ around [...] people. It is anticipated that over the five initial years, the parent companies will invest US\$ [...] billion (ECU [...] billion) in Newco including the assets which will be transferred to it prior to closing. BT will invest US\$ [...] million and MCI US\$ [...] million.

(ii) Purpose and activities of Newco

- (23) Newco has been created for the provision of enhanced and value-added telecommunications

services and outsourcing to big companies. By enhanced and value-added telecommunication services the parties mean any international telecommunication service (collectively referred to as global products) which the regulatory framework permits to be offered between two or more countries by members of a single group and which the regulatory framework permits to be managed on an end-to-end basis⁽¹⁾.

To achieve that goal, Newco's precise activities can be split into planning and management on the one hand, and support and marketing on the other hand.

1. Provisions concerning planning and management

In respect of planning and management activities, Newco will be responsible for :

- (a) the planning and development of global products. As part of this function, Newco will review the current products of the parent companies and the regulatory constraints still existing at any given moment ;
- (b) the establishment of a global platform (i.e. a software package) over which the global products will be provided. Newco will provide a 'best-of-breed' platform comprised of a combination of any or all of transmission, switching, signalling, network intelligence and service management services. The architecture, design and continuing development shall be at the discretion of Newco, although it shall ensure that those parts of the distributor domestic system used are compatible with the overall design. Such platform will be based initially on the existing systems of the parent companies. Thus interworking those systems will consume the most important part of Newco's time and efforts in its early years of operation ;
- (c) the provision of telecommunications services management to customers, including the acquisition and management of assets and staff from customers (global outsourcing)⁽²⁾.

⁽¹⁾ The following services are excluded from the definition : (i) voice international simple resale (ii) international direct distance dialling provided on a correspondent basis (iii) the provision of international private leased circuits and (iv) any services which for regulatory reasons must be offered on a correspondent basis.

⁽²⁾ In this respect, Syncordia, BT's existing outsourcing unit, will continue to exist, either as a division or as a separate branch within Newco.

In order to carry out the foregoing, Newco will have a budget for R&D activities. However, as Newco will not have its own in-house facilities, the R&D activities will actually be undertaken mainly by the parent companies, under contract with Newco. The former will keep the ownership of their laboratories and of the existing technology being licensed to Newco.

2. Support and marketing

Newco will derive its revenue from selling its services to its parent companies who will be the exclusive distributors of the Newco products. In this respect, it will not have direct contact with customers except as regards the provision and sale of global outsourcing services. Newco will nevertheless have a number of responsibilities and obligations towards the distributors :

- (a) it will decide, according to principles set out in the business plan, who is going to be the main or 'lead' distributor in each contract for global products ;
- (b) it will provide technical and commercial support to each distributor in sales and marketing activities including assisting in identifying potential customers, advising on the most suitable means of meeting the requirements of a customer, supporting account management and assisting in the preparation of proposals to customers ;
- (c) it will provide billing services to distributors ;
- (d) it will provide second-level customer service in support of the first-level support provided by the distributors ;
- (e) it will carry out global market analysis and an annual products development plan.

(iii) Provisions concerning dealings with/by Newco

- (24) Pursuant to Article 17 (1) of the JVA, transactions between Newco and a shareholder are to be on terms and conditions substantially as favourable to Newco as if such transaction had been entered into with a third party on an arm's-length basis (cost plus a reasonable market rate of return) but no more than that.

Pursuant to Article 17 (3) of the JVA, Newco is to purchase all products, services and facilities from

the parent companies only if in each case the relevant parent company can provide the same on terms at least as favourable as regards price, quality and service to Newco as would be obtainable in an arm's-length transaction from a supplier not related to Newco or the parent companies.

(iv) Non-compete provisions

- (25) Pursuant to Article 18 (1) (a) of the JVA, and except in accordance with the DA, each shareholder and its ultimate parent company undertakes to Newco and the other shareholder and its ultimate parent company that it will not carry on or be engaged or interested in the provision of enhanced and value-added telecommunication services anywhere in the world or international outsourcing services or appoint any person to be a director of a business which provides such services other than as director of Newco or its subsidiary undertakings. In addition, and except in accordance with the distribution agreement, they also undertake not to solicit the custom of any person for the purpose of offering to it enhanced and value-added telecommunication services or international outsourcing services.

However, neither BT nor MCI will be in breach of the non-compete provision as a consequence of any actions undertaken by either of them in compliance with the licence granted to BT by the Secretary of State, or any applicable regulatory certificate, licence or any obligation imposed upon MCI by any authority in the United States of America (Articles 18 (3) and 18 (4) of the JVA). It has to be noted, however, that in such a case, and provided that the parent company involved cannot find an alternative means of complying with the non-compete provision, it shall pay to Newco an amount equal to any profits made as a result of such action (Article 18 (5) of the JVA).

Finally, Articles 18 (9) and 18 (10) of the JVA ensure that in the case of deregulation of the US/UK (and vice versa) route for the provision of international voice services, BT and MCI will receive from each other the necessary support to compete ; however, if the two parent companies cannot agree on a method to effectively compete with third parties except by means of international voice resale, then Newco will be authorized to offer basic international voice services on that deregulated route. As indicated in recital 11 should this occur, a new notification will be required.

(v) Licences granted to Newco and by Newco to the distributors

(26) Pursuant to Article 3 (3) of the ITA, each parent company grants to Newco irrevocable, perpetual, non-exclusive, non-transferable licences to use the technical information solely for the purposes of the business. However, it has to be noted that the term 'technical information' excludes confidential information (the sharing of which between and among the parties is substantially restricted by the terms of a Data Segregation Schedule of the JVA) and trade secrets of a commercial nature.

Newco has the right to grant the following sublicences to its parent companies :

(a) to BT solely for its territory (i.e. the world excluding the Americas) and to MCI solely for the Americas, to use the technical information licensed from the parent companies in the distribution of Newco's products (Article 3 (4) (a) (i) of the IPA). In addition, each distributor has the right to grant similar sub-sublicences to customers and an outside party for the sole purpose of discharging, in whole or in part, the licensed distributor's obligations under the relevant distribution agreement (but in any event restricted to the territory of that distributor);

(b) to the so-called non-owning parent company (i.e. the parent company that does not own a specific technical intellectual property right), to use the licensed technical information in respect of products other than global products provided by Newco to customers connected to/or served by such parent company but limited to that parent company's territory as distributor (Article 3 (4) (c) of the IPA).

Newco itself cannot sublicense an outside party with two exceptions :

(a) where the distribution agreement has become non-exclusive (Article 3 (5) (a) of the IPA);

(b) where Newco is providing directly to any customer global outsourcing directly to any customer.

Furthermore, Newco grants to each parent company, upon request, similar licences to use the technical intellectual property rights (Article 6 of the IPA) of Newco.

Finally, it has to be noted that the sublicences granted to BT or to MCI under their respective technical intellectual property rights will survive

termination of the agreement as irrevocable, perpetual and worldwide licences unrestricted as to use and licensing (Article 13 (1) (b) and 13 (2) (b) of the IPA), subject only to the payment by each parent company to the other of a given royalty during four years. In addition, they also receive similar licences for Newco's own intellectual property rights.

(vi) Ownership by Newco of new technology

(27) Pursuant to Article 7 (1) of the IPA, Newco may be the owner of the technical intellectual property rights in new developments. In such a case, and assuming that a given development was actually made by one parent company under contract by Newco, such parent company (Newco does not have its own R&D activities) will receive from Newco a non-exclusive, irrevocable, perpetual licence to use that development for any purpose (Article 7 (2) of the IPA). Conversely, where the new development is owned by the parent company that effected it, that parent company will grant a similar licence to Newco (Article 7 (3) of the IPA).

(vii) Trade mark provisions

(28) Pursuant to Article 12 (3) (a) and (b) of the IPA each parent company grants the other (this time without any intervention by Newco) a non-exclusive licence to use and license the trade marks of the one in the territory of the other in connection with the sale, distribution, provision or performance of global products only.

(viii) Provisions regarding the distribution of Newco products

(29) Pursuant to Article 2 (1) of each DA, Newco appoints the distributor as its exclusive distributor in the territory. Such appointment means that the distributor has the exclusive right to promote, sell and distribute services in the territory (Article 3 (1) of the DA) and the corresponding obligation to promote the sale of the global products in the territory (Article 8 (1)). In addition, the distributor agrees to obtain from Newco, with some exceptions, all requirements for global products (Article 5 (1)). Finally, in consideration of the provision of the services, the distributor pays to Newco (i) a variable annual charge based on the forecast that each distributor is obliged to provide to Newco each

year of the aggregate requirements of its own customers for the following 12 months⁽¹⁾, and (ii) a usage charge. Also, in consideration of the licences granted by Newco to the distributor pursuant to the intellectual property agreement, the distributor shall pay Newco an annual charge that for the first financial year will amount to US\$ 6,5 million (Article 16).

Newco undertakes not to sell global products directly or indirectly in the territory other than to the distributor (Article 4 (1)). However, Newco can sell global outsourcing services directly to customers when it is desirable to do so for tax or other reasons and assuming that in such a case the distributor releases Newco from its undertaking in Article 4 (1) (Article 4 (2)). The provision of the global products to the distributor includes the provision by Newco of all necessary use of remote networks on the most competitive terms available, where the products are to be provided at one or more sites of one customer located outside the territory (Article 6 (5)), and the provision by Newco of reasonable technical and commercial support to the distributor in sales and marketing activities (Article 9).

B. Concerning BT's investment in MCI

(i) Restriction on transfer of shares by BT and limits to the ability of BT to increase its shareholding in MCI

- (30) Pursuant to Article 5 (1) of the IA, BT undertakes not to dispose of its shares in any manner whatsoever for four years from the closing date. After that date, BT can sell, but must give a right of first refusal to MCI (Article 5 (3) of the IA).

Pursuant to Article 6 (1) of the IA, BT is granted the right to acquire any new shares issued by MCI necessary to maintain the percentage it has in MCI at that time or to increase it assuming that such purchase does not breach any foreign ownership restrictions under US law applicable at the relevant time (Articles 6 (2) (d) and 6 (4) of the IA).

However, pursuant to under Article 7 (1) of the IA, BT has agreed not to acquire, directly or indirectly, the ownership of any additional equity of MCI to exceed 20% thereof until the 10th anniversary of the closing date. Furthermore, during the same

⁽¹⁾ It has to be noted that if the actual requirements of the distributor are less than those stated in the forecast, no part of the charge will be refunded by Newco.

period, BT has expressly undertaken not to seek to control or influence the company (Article 7 (3) of the IA).

Once the 10-year 'standstill' period has expired, BT can increase its shareholding up to the level then fixed by the US Communications Act as regards foreign ownership. However, even if those restrictions were completely eliminated, BT would generally only be allowed to exceed a 35 % stake in MCI by a tender offer or business combination that has been approved by a majority of the independent directors and by a majority of the shareholders (other than BT) (Article 7 (4) of the IA).

(ii) BT's consent rights and board representation

- (31) The MCI board is to be composed of 15 directors. BT's representation on the MCI board will remain in proportion to its shareholding. BT is currently entitled to three directors. Four directors can be executive officers of MCI. There is a similar representation on most MCI board committees. At least eight members of the MCI board must be fully independent of MCI and BT (Articles 9 (7) and 9 (9) of the IA).

BT, as the sole holder of MCI's class A common stock, has been granted substantial consent rights with respect to certain corporate actions of MCI concerning equity issuances, acquisition of core and of non-core business, sales of assets and borrowing above certain specified limits.

(iii) Loss of rights provisions

- (32) Pursuant to Article 9 (12) of the IA, in the event that either BT or MCI engages, directly or indirectly, in the core business⁽²⁾ of the other (in the Americas in the case of BT and outside the Americas in the case of MCI) or transfers or provides sales and marketing in connection with any person or acquires an interest in any person who is engaged in the core business of the other, then the engaging party will lose certain rights.

⁽²⁾ Defined as all telecommunications and other electronic information services and equipment for the provision of such services, as they exist on the date of this agreement or hereafter exist, including (but not limited to) all forms of telecommunication access and egress; and value-added consumer and business services generated through or as a result of underlying telecommunications services using all technology (voice, data and image) and physical transport, network intelligence, and software applications, and including (i) information processing, (ii) systems integration and outsourcing, (iii) transaction processing and (iv) cable television.

In the case of BT, its shares in MCI will be converted into common stock and it will lose its voting and consent rights and its board representation in MCI.

In the case of MCI, BT will cease to be bound by various obligations concerning future share transfers, voting or the standstill provisions mentioned above.

In any event, the loss of rights provisions will not be automatically triggered; there are a number of exceptions (listed in Article 9 (12) (b) and (d) which include without limitation correspondent relationships in the ordinary course of business and any activities in connection with the ownership of Newco) and a procedure to be followed (including arbitration in case of disagreement) before a loss of rights is deemed to exist.

E. THIRD PARTY OBSERVATIONS

- (33) Following the publication of a notice pursuant to Article 19 (3) of Regulation 17 and to Article 3 of Protocol 21 of the EEA Agreement, comments were received from two interested third parties. One of them requested its comments and identity to remain confidential. The other set of comments received focused on the ability of BT to distort competition in the provision of enhanced and value-added services throughout Europe, given its control of local access facilities in the United Kingdom and on the necessity for the Commission to impose undertakings on the parties with respect to non-discriminatory treatment of competitors and cross-subsidization of competitive services with revenues derived from non-competitive operations, to facilitate the development of effective competition in the telecommunications market.

The Commission studied carefully the comments received and concluded that concerns expressed by those third parties had already been raised by the Commission and discussed in detail with BT and MCI, who had provided adequate answers and safeguards. Consequently, those comments have not caused the Commission to modify its substantive position indicated in the Article 19 (3) notice and expressed below, as regards the notified agreements.

II. LEGAL ASSESSMENT

A. APPLICATION OF ARTICLES 85 (1) OF THE EC TREATY AND 53 (1) OF THE EEA AGREEMENT TO THE CREATION OF NEWCO AND TO BT'S INVESTMENT IN MCI

1. The creation of Newco

(a) *Competition between the parent companies and/or Newco*

- (34) The parent companies must be considered potential competitors of Newco and of each other in respect of the global products to be offered by Newco and actual competitors in the overall telecommunications market.

The inherent evolving nature of the business scope of Newco will have an effect on the issue of potential/actual competition; it is therefore considered that when (and if) Newco begins to offer some basic services (recital 11), the parent companies will become actual competitors of Newco.

- (35) The abovementioned conclusions are based on the following arguments:

(a.a) potential competition in international value-added and enhanced services

- (36) Newco's offering will consist of a mixture of the parent companies' existing products and networks. Prior to the incorporation of Newco, the parent companies were competitors, at least to a limited extent, for obtaining contracts for similar sets of products and services. Thus, BT won a contract with Hewlett Packard North America for the development of a global communications strategy focused mainly on Europe and Asia Pacific. In addition, customers of MCI for value-added services in the United States of America with branches abroad could obtain basically the same features (with some limitations depending on the number of locations abroad) in respect of these value-added services when entering into contact with their facilities abroad as when doing the same in the United States of America. Although many of those services are provided on a correspondent basis — i.e. by means of connecting MCI to another TO's network — some of them — MCI mail, for instance — are provided on a non-correspondent basis.

- (37) The parties have indicated that they have withdrawn from the market that Newco will address. However, Newco has in fact received a licence from the parent companies to use the technologies and the latter retain the ownership of their respective know-how and intellectual property rights and also keep intact their respective R&D capabilities.

Newco will not do any research and development on its own but will award contracts mainly to its parent companies to do so. It is therefore considered that the parent companies will certainly keep and increase their proficiency and know-how in respect of the technologies required to stay in (or to re-enter) the market.

In addition, although the ownership of any new development could be awarded to Newco, it is possible (depending on the specific arrangements made in each case) that the developing parent company obtains the ownership, and, in any event, the parent companies will receive licences from Newco for using any such developed technology for any non-global product.

- (38) The parties have declared that they intend to offer to their intranational customers (that will usually be the national facilities of Newco's international customers) a set of services that for the customers will have an identical look and feel to the services offered by Newco in the international arena. For so doing they will receive from the other parent company through Newco the appropriate licences. Neither BT nor MCI are prevented, within their own territories, from setting up local subsidiaries in any given country to serve the local needs of companies in those countries. As a result a customer could be contracting at the same time with BT (or MCI), outside Newco, for its local needs and with BT (or MCI) as exclusive distributor of Newco for the customer's international needs.
- (39) Furthermore, customers may be international, but have such a concentration of traffic in either the United Kingdom or the United States of America that the relevant parent company's offering could be in direct competition with that of Newco were the customer to decide to forego Newco's international spread in order to get a good deal on domestic telecommunications which formed the bulk of its needs.
- (40) Finally, the parent companies will maintain their commercial presence and reputation intact. They

will also keep, in particular because they will be the exclusive distributors of Newco, and increase their knowledge of the market in terms, for instance, of customers' needs.

All the above elements make the probability of such a (re)entry more credible.

(a.b) Actual or at least potential competition in the overall market for telecommunications services

- (41) BT and MCI are the fourth and fifth largest telecommunications companies in the world in terms of traffic. BT, as the former monopolist in the United Kingdom, still keeps a very substantial amount of market power in that Member State as reflected by BT's overall market share (around 90 % of the UK market). MCI is the second largest long-distance carrier in the United States of America, although significantly behind AT&T.

Under a traditional approach based on the state of international telecommunications prior to liberalization, TOs were limited to activities on their respective domestic markets and thus did not compete. However, this view cannot be maintained any longer, at least as far as large users of telecommunications are concerned. The different networks compete on features and prices for the installation of the telecommunication hubs of those large users. The intensity of this competition is bound to increase in the coming years as long as the liberalization process continues.

- (42) Both MCI and BT develop direct activities outside their home markets by means of subsidiaries and/or their activities in international organizations.

MCI employs 150 people in Europe and has several subsidiaries in different Member States (Germany, Belgium, France, Italy and the United Kingdom). Those subsidiaries provide the liaison office with the local TO involved, and also provide maintenance and repair of customer-based equipment, and coordination of billing information with multinational customers. They also support the sale of several of MCI's services (i.e. MCI Call USA, Vnet) which are available to European users and in competition with international direct dial services offered by BT or by other TOs in their respective home markets. Apart from the subsidiaries already mentioned, MCI has a branch office in the United Kingdom, MCI Ltd, to hold the name only, and

another in the Netherlands, MCI Global Ventures BV, intended to be the holding company of a project that did not materialize. In addition, in Greece, Ireland, Spain and the Netherlands, MCI conducts liaison activities and sales support for services through independent contractors.

MCI currently provides enhanced private line services between the United States of America and the United Kingdom pursuant to a telecommunications services licence in the United Kingdom. In addition, MCI also provides data-only services for one customer's worldwide reservation system using VSAT licences issued in Germany and France to Overseas Telecommunications Inc., an MCI subsidiary.

Finally, MCI has a 8,5 % participation in the Financial Network Association (FNA), an association formed for the purpose of helping the supply, on a correspondent basis, of specialized telecommunication services to the global financial community. In addition, MCI had a 25 % stake in Infonet, but has divested itself thereof.

BT has substantial activities in some Member States, in particular, France, the Netherlands, Germany and Spain (where it has recently created, together with the Spanish Banco de Santander, a joint venture to offer data services in Spain). However, the bulk of BT's activities abroad prior to the transaction with MCI was in the United States of America. As a result of the operation, most of British Telecom North America (BTNA) activities will be sold to MCI, and Syncordia will be transferred to Newco. Nonetheless, BT will keep a residual staff presence in the United States of America and BT USA Holdings, the US holding company. Apart from these, BT will retain BT US Capital Corporation (which is used by BT for obtaining funds in the US market), BT US Paging Inc., BT US Ventures Inc. and BT US Cableships. Finally, BT has held a 25 % shareholding in McCaw but this has now been sold to AT&T in exchange for 2 % of the outstanding voting power of AT&T, worth in the region of US\$ 2 billion, which does not give BT any influence over AT&T's commercial strategy and which BT has declared it expects to sell at the appropriate time.

(b) *Applicability of Article 85 of the EC Treaty and Article 53 of the EEA Agreement to the creation of Newco*

(43) Having concluded that BT and MCI are, and for the foreseeable future will continue to be, at least potential competitors in the two markets concerned, it is necessary to assess whether the creation by them of Newco falls under Article 85 (1).

It has not been demonstrated conclusively that the creation of Newco is the only objective means for the parent companies to enter and stay in the market for international and enhanced value-added services, because both parent companies are companies that currently have substantial activities in similar fields, including the provision of services to customers abroad, sometimes on a non-correspondent basis, and that have the financial and technological capacities required to enter the relevant market on their own. In doing so, they will be facing substantially the same constraints, in terms, for instance, of regulation, that Newco will be facing, when trying to enter the relevant market. In addition, the creation of Newco means that each parent company is unlikely itself to develop a similar set of products for use in the relevant market on its own. For these reasons, the creation of Newco falls within the scope of Article 85 (1) of the EC Treaty and Article 53 (1) of the EEA Agreement.

In addition, under its present structure, Newco can be considered as a vehicle for the parent companies to pool their respective intellectual property rights and to cross-license each other and Newco on an exclusive basis as far as the services to be offered by Newco are concerned, given in particular the non-compete provision, but also given the intellectual property agreements, the geographical scope of the licences granted to Newco by the parent companies and by Newco to them, and the terms of the exclusive distribution agreements. The Commission has indicated, in respect of reciprocal licences between competitors on an exclusive basis, that the benefits of the block exemption regulations on patent and know-how licence agreements to such licences are conferred only if the parties are not subject to any territorial restriction within the Community, including restrictions that isolate the Community against imports from non-member countries and thereby adversely affect the conditions of competition within the Community.

For the abovementioned reasons it is concluded that Newco falls within the scope of Article 85 (1) of the EC Treaty and of Article 53 (1) of the EEA Agreement.

2. BT's investment in MCI

- (44) As a general rule, both the Commission and the Court of Justice have taken the view in the past that Article 85 (1) does not apply to agreements for the sale or purchase of shares⁽¹⁾ as such. However, it might do so, given the specific contractual and market contexts of each case, if the competitive behaviour of the parties is to be coordinated or influenced.

The Commission consequently assessed whether the presence of BT's nominees to the board of MCI could give rise to coordination of the competitive behaviour of the two companies, in particular given the access that BT will have to MCI's confidential information. In this respect, the IA has been drafted in such a way that BT does not have the possibility to seek to control or influence the company. This is particularly so in the case of the obligations found in Articles 7 (1) (not to increase shareholding for 10 years) and 7 (3) (not to seek to control or influence the company).

In addition both American corporate and antitrust laws would impede any misuse of (or even the access to) any piece of confidential information of MCI by BT.

For the reasons mentioned above, it is concluded that the investment by BT in MCI does not fall within the scope of Article 85 (1) of the EC Treaty or Article 53 (1) of the EEA Agreement.

B. APPLICATION OF ARTICLE 85 (1) OF THE EC TREATY AND ARTICLE 53 (1) OF THE EEA AGREEMENT TO CONTRACTUAL PROVISIONS

- (45) The following provisions restrict competition :
- (a) the appointment of BT as exclusive distributor of Newco (Article 2 (1) of BT's DA) within the EEA ;
 - (b) the obligation on the parties to obtain from Newco all requirements for global products (Article 3 (1) of each DA) ;
 - (c) the non-compete provision as regards the activities of Newco (Article 18 (1) of the JVA) ;
 - (d) the 'loss of rights' provisions pursuant to Article 9 (12) (c) of the IA, as regards the activities of MCI in the territory of the EEA.

⁽¹⁾ See the Decision in Philip Morris/Rembrandt/Rothmans referred to the 14th Report on Competition, points 98 to 100 and Joined Cases 142/84 and 156/84, BAT and Reynolds v. Commission, [1987] ECR 4487.

- (46) Of these restrictions, the non-compete provision and the obligation to buy all requirements for global products from Newco are ancillary to the creation and successful initial operation of Newco. In this respect, they are considered to be subsumed under the joint venture and, consequently, they will not be assessed pursuant to Article 85 (1) of the EC Treaty and Article 53 (1) of the EEA Agreement separately from the joint venture itself.

Newco is the way chosen by BT and MCI to enter the relevant market. In this respect, both restraints are different expressions of the same firm commitment made by the two parent companies towards each other and towards Newco, and required for Newco to successfully enter the market, considering the characteristics of the emerging market for global value-added and enhanced services (and those of the overall market for telecommunications), in terms of uncertainty and associated risks, substantial investments required, and level of competition from similar ventures. Those characteristics are reflected in the fact that Newco is expected to incur substantial losses at least during its early years of operation.

The non-compete clause is aimed at ensuring that BT and MCI will concentrate their efforts on Newco, as regards the services to be offered by the joint venture ; thus parallel activities by them (for instance in cooperation with other TOs) do not frustrate Newco's success in entering the relevant market.

The obligation on BT and MCI, as the exclusive distributors of Newco, to buy all requirements for global products from Newco, is aimed at ensuring a steady stream of funds for Newco and at increasing the credibility and market reputation of Newco ; if the parent companies were free to obtain global products from other sources, in particular in cases where Newco could adequately satisfy a particular requirement, that might severely affect the credibility of Newco and its financial position. It has also to be noted that Newco itself is not obliged to obtain from its parent companies all of its requirements for telecommunications and other products and services.

Ancillary provisions are usually accepted for a limited period of time. In the present case, however, in view of the particular circumstances of the market in which Newco will be operating, including the substantial investments involved and the associated risks, those provisions will be accepted as ancillary for the entire duration of the exemption granted by this Decision to the joint venture.

- (47) The appointment of BT as exclusive distributor of Newco within the EEA falls under Article 85 (1) of the Treaty and under Article 53 (1) of the EEA Agreement because it has as its object or produces as its effect the isolation of the EEA against imports of the relevant services, as offered by Newco, from outside the EEA. Such fact will adversely affect the conditions of competition within the EEA. In addition, it cannot be considered ancillary to the creation of the joint venture taking in particular into account that the agreements foresee the possibility of the distribution becoming non-exclusive (Article 3 (5) (a) of the IPA).

As to the appointment of BT as exclusive distributor of Newco in the BT territory outside the EEA territory and the corresponding provision under MCI's distribution agreement concerning the Americas, these provisions do not produce any appreciable effect in the EEA. For that reason they do not fall under either Article 85 (1) of the EC Treaty or Article 53 (1) of the EEA Agreement.

- (48) In view of the current state of development of the overall market for telecommunications, the 'loss of rights' provision affecting BT (Article 9 (12) (a) of the IA) and, in so far as the territory of the EEA is not concerned, the 'loss of rights' provision affecting MCI (Article 9 (12) (c) of the IA), will not produce any appreciable effect in the EEA. For that reason these provisions do not fall under either Article 85 (1) of the Treaty or Article 53 (1) of the EEA Agreement.

On the contrary, in so far as the territory of the EEA is concerned, the 'loss of rights' provision pursuant to Article 9 (12) (c), already has an appreciable effect in the EEA and cannot be considered ancillary either to the investment of BT in MCI or the incorporation of Newco. It has as its object or produces the effect of significantly impeding any entry by MCI into the territory of the EEA using its existing technologies, in segments of the telecommunications market, that are currently outside the business scope of Newco but within the widely defined 'core business' of BT. In this respect, this provision, although it is not a non-compete provision as such, because MCI is not actually prevented from competing on its own in BT's territory (the effect of the provision is to make MCI pay a high price in case it decides to compete with BT in fields different from those covered by Newco), will nevertheless produce a practical effect very close to a non-compete obligation.

As a result, MCI might for instance in practice feel dissuaded from setting up a local company in any country within BT's territory to provide non-international value-added services, even though only using its existing range of products and services (that is, without infringing any intellectual property right belonging to BT or to Newco), within that country.

Any agreement which presents undertakings in third countries from becoming suppliers or competitors within the Community falls within the scope of Article 85 (1) of the Treaty (and under Article 53 (1) of the EEA Agreement). The assessment of the case has not shown the existence of any reason that would justify departing from that established practice.

In addition, a non-compete provision that extends beyond the field of activity of a joint venture cannot be accepted as such⁽¹⁾.

For those reasons, the 'loss of rights' provision for MCI pursuant to Article 9 (12) (c) of the IA falls under Article 85 (1) of the Treaty (and Article 53 (1) of the EEA Agreement) in so far as the territory of the EEA is concerned.

C. EFFECT ON TRADE BETWEEN MEMBER STATES AND BETWEEN MEMBER STATES AND EFTA COUNTRIES

- (49) In point 39 (i) of the Guidelines on the application of EEC competition rules in the telecommunications sector⁽²⁾ issued by the Commission, it is stated that as in the entire Community non-reserved services, equipment and space segment infrastructure are traded, any agreement concerning them may affect trade between Member States. This is the situation in the present case as Newco will cover the provision of value-added services not only between the EEA and abroad, but also between any two EEA countries. Such effect on trade between Member States, and between Member States and the EFTA countries, is going to be substantial in view of the growing size of the market, and of the further expansion expected for the coming years.

⁽¹⁾ See Article 3 (3) of Commission Regulation (EEC) No 2349/84, Article 6 (a) of Commission Regulation (EEC) No 418/85 and Article 3 (5) of Commission Regulation (EEC) No 556/89.
⁽²⁾ OJ No C 233, 6. 9. 1991, p. 2.

As regards non-ancillary provisions, they also affect trade between Member States, and between Member States and the EFTA countries, because they tend to insulate the entire EEA by impeding the development of existing or new activities by MCI within it, not only in respect of the products and the geographic areas within the business scope of Newco (as a result of the exclusive distribution arrangements) but also in respect of products or geographic areas that are outside the business scope of Newco (as a result of the 'loss of rights' for MCI).

As the provision of services between any two EEA countries is included in the business scope of Newco, such effect on trade is substantial.

D. CONCLUSION IN RESPECT OF ARTICLE 85 (1) OF THE EC TREATY AND OF ARTICLE 53 (1) OF THE EEA AGREEMENT

- (50) In conclusion it is considered that the creation of Newco falls under Article 85 (1) of the Treaty and Article 53 (1) of the EEA Agreement, and that this is also the case of the non-ancillary provisions mentioned above. The restrictive effect on competition and on trade between Member States is considered to be substantial.

E. APPLICATION OF ARTICLE 85 (3) OF THE EC TREATY AND ARTICLE 53 (3) OF THE EEA AGREEMENT

- (51) The objectives of the parent companies in entering this set of transactions are somewhat different. BT wants to become a leading global provider of international value-added and enhanced telecommunications services in the world, but with a particular emphasis in Europe and in the United States of America. Collaboration with a major American player was particularly important for BT to achieve those goals, and in particular to enter the US market, where 40 % of multinational companies are located.

MCI's main interest was to maintain its competitive position in the Americas, in particular against AT & T. In order to do so, as customers' demand for global services was increasing, MCI considered it necessary to add a global dimension to its services but without having to establish itself abroad; it therefore chose the joint venture alternative. MCI first entered into Infonet, but finally opted for an alliance with another TO. In this respect, after negotiating with different TO's it turned to BT. As a result of the transactions it will

obtain the financial means to finance the improvement of its infrastructure in the United States of America.

- (52) The agreements notified, in so far as they fall under Article 85 (1) of the EC Treaty and Article 53 (1) of the EEA Agreement, satisfy the conditions for exemption laid down in Article 85 (3) of the Treaty and Article 53 (3) of the EEA Agreement.

(a) Improvements

- (53) It is considered that Newco will improve telecommunications services and technical/economic progress in the Community in the following ways:

— The combination of BT and MCI technologies will allow Newco to offer new services, based on the existing services of the parent companies, more quickly, cheaply and of a more advanced nature than either BT or MCI would have been capable of providing alone under their existing technologies. Such combination will nevertheless require a very costly and time consuming effort as demonstrated by the fact that the set of services that Newco will offer will not be fully operational within five years. In addition, as a related consequence, MCI technology, which is said to be one of the most credible and user friendly in the world, will be made available to European customers of Newco (within the limits imposed by the non-ancillary provisions to be discussed below).

— The strategy of Newco for entering the market is to add value to basic transmission capacity (international private leased lines) obtained from local TOs. However, Newco will not use the features of each national network involved but will instead add its own switching systems, call processing/routing, signalling and databases as well as software to provide the international services on a truly seamless basis. This is considered to be a real advantage over existing international services that are provided (this is the case of BT and MCI) by interconnecting national networks that are usually incompatible in terms of structure, software, hardware and management systems. The result of a combined network so creative, is as strong as its weakest link and so the number of services and the features thereof are those supported by the less performant national network involved.

— In addition, if successful, Newco could allow the Community's most important companies to achieve levels of telecommunications performance on an international level currently only available at some national/local levels, that

could enable them to better withstand global competition from other corporations operating from parts of the world where technological advance in telecommunications is becoming common-place.

- Finally, Newco will allow cost savings resulting from its operation of a single network architecture reflecting economies of scale at a technological and operational level, and possibly from cheaper interconnections obtained from TOs given Newco's expected size. In this respect, Newco will no doubt generate competition between the providers of international basic transmission capacity in order to obtain the lowest costs for its business, and will try to direct traffic over alternative routes in order to achieve the lowest cost routing available.

- (54) Both the exclusive distribution arrangements in respect of BT and the 'loss of rights' for MCI as regards the EEA, are aimed at ensuring that each parent company concentrates its marketing efforts, in terms of prospecting for customers, investments on regional and/or national networks and other facilities, within its respective territory, as required by a successful market entry by Newco. At the same time, Newco will benefit from the reputation and track-record of its parent companies, *vis-a-vis* its potential customers.

(b) Consumers

- (55) The incorporation of Newco will mean that consumers in general will benefit more rapidly from a set of new advanced services than Newco's parent companies would have been capable of providing separately.

In addition, consumers, big companies in this case, will benefit directly through the provision of :

- a greater product portfolio of developed and new services allowing them to operate more effectively on a global scale and to better compete with their global as well as with their Community and EEA competitors, and
- lower pricing resulting from the cost savings to be made by Newco as a result of operational efficiencies or pressure on local TOs.

Such advantages will improve the competitive position of those company users in their respective markets, in particular against competitors that have at their disposal more advanced telecommunications.

In this respect, the exclusive distribution arrangements for BT will ensure in respect of its customers that there is a single person to contact in case of any kind of difficulties related to the continuous provision of the services anywhere in the world. In addition, the 'loss of rights' for MCI, seen as a means of permitting confidence between the parent companies to grow (see recital 62) would guarantee the necessary stability of the underlying relationship between BT and MCI necessary for it to be successful. A successful entry by Newco will increase the level of competition in the relevant market, and hence the possibilities of choice available for customers. Such stability is also a very important element for customers when considering giving a potential supplier responsibility over a strategic element as to their telecommunications needs.

(c) Remaining competition

- (56) The creation of Newco will not afford the parties the possibility of eliminating competition in respect of the categories of services to be offered by Newco. Such conclusion is also applicable to the non-ancillary restrictions identified above, and is based on the following arguments :

- At Newco's level there will be significant third-party competition coming first of all from AT & T's Worldsource and from Eunectom (or from any enhancement of Eunectom if plans for a closer cooperation between Deutsche Bundespost Telekom and France Télécom go ahead). There will also be competition from other existing alliances, such as Unisource or IPSP, or from alliances to be concluded between TOs that have not taken a position until now (like Sprint, and the 'Baby Bells' in the United States of America, NTT in Japan and some significant European TOs like Telefónica, Belgacom, Mercury or STET). Finally, the parties also expect competition, at least for components of global value-added telecommunications services, coming from other players including computer and data processing companies (like IBM, DEC and EDS) and information service companies (like Geis and Compuserve).

- Multinational or other big companies are sophisticated purchasers with the ability to build their own private network solutions or to attract offers from competitors of Newco. This gives the multinationals considerable bargaining power reflected in intense pressure on margins, and competition between the suppliers for customers.

- (57) In this context, the Commission has examined in detail and discussed with the parties, the extent to which access to MCI and BT networks by third parties is possible. This is an important question that can become of particular relevance in the near future, as is also the issue of possible cross-subsidization of Newco by BT, an issue that the Commission has also examined in detail.

In this respect, existing regulation to which BT and/or MCI are subjected in their respective countries prevents such cross-subsidization and/or discrimination from taking place.

As regards MCI, under the requirements of the Communications Act of 1934, as enforced by the Federal Communication Commission (FCC), MCI's network arrangements and services are described in publicly available tariff schedules or contracts.

The Communications Act and the FCC's policies prohibit MCI from making any unjust or unreasonable discrimination in the provision of its services including access to these services by MCI's competitors and foreign correspondents. In addition the FCC has a complaint process, should any party feel aggrieved by MCI's actions or inactions (or by those of any other TO in the United States of America).

The situation is similar as regards BT because under the terms of the Public Telecommunications Operator Licence that BT received under the Telecommunication Act 1984, which is enforced by the Office of Telecommunications (OfTel), BT cannot show undue preference or discrimination in the provision of certain services towards other persons, nor unfairly favour any part of its own business against competitors. In addition, a prohibition on exclusive dealing in the provision of international telecommunications services prevents BT from making arrangements with overseas correspondents, including MCI, which would exclude them from dealing with other operators in the United Kingdom. Finally, condition 18 of BT's licence (together with condition 38, in so far as the confidentiality of customer information is concerned⁽¹⁾), empowers OfTel to act against any unfair cross-subsidy by BT and imposes upon BT an obligation

to keep records of any material transfer between any parts of its business.

Those regulatory constraints are reflected in the agreements, so that actions undertaken by MCI or BT in complying with their respective obligations are excluded from the non-compete provision in the JJVA (Articles 18 (3) and 18 (4)) and from the 'loss of rights' provisions in the IA (Articles 9 (12) (b) (iii) and 9 (12) (c) (iiii)).

The abovementioned regulatory constraints, together with the additional explanations provided by the parties, have permitted the Commission to conclude that it is not necessary for it to take any further action as of now, including requesting the parties to make appropriate undertakings to the effect that they will neither discriminate nor cross-subsidize. However, should this conclusion prove to be wrong in the future, the Commission will immediately apply the competition rules of the EC Treaty (and if applicable those of EEA Agreement) as required.

(d) Indispensability

(i) *Newco*

- (58) The formation of *Newco* itself is indispensable for the parent companies to successfully enter the relevant market :

— *Newco* will allow the time required for the relevant services to be marketed to be substantially shortened. As many other companies (mainly alliances) are entering the relevant market, the time required for being in the market with a comprehensive set of services is a competitive factor of the utmost importance.

— In addition, *Newco* will allow each parent company to substantially reduce the costs and risks inherently associated with the complex organization required to offer such services at the scale and with the other features required by multinationals and other big international users.

— Finally, as indicated in recital 7, *Newco* is a means to quickly overcome the inadequacies associated with the provision of the services and features (one-stop-shop, end-to-end and seamless basis, etc.) required by multinationals and other big international users, under the existing framework of cooperative relationships established by TOs.

⁽¹⁾ The use of such information is also restricted by the Data Segregation Schedule of the JVA, to which reference is made in recital 26.

(ii) *Exclusive distribution*

- (59) Under BT's distribution agreement, BT is appointed by Newco as the exclusive distributor for Newco's products in a wide territory, covering the entire world excluding the Americas.

Such exclusivity is reinforced by the licensing provisions in the IPA. Thus, pursuant to Article 3 (4) (a) (i), Newco sublicenses BT solely for the 'territory' and MCI solely for the Americas to use the combined technology it has received from its parent companies in the distribution of Newco's products. In addition, each parent company (or distributor) receives directly from the other a non-exclusive licence to use and license the trademarks of the latter within its own territory. Thus, BT grants MCI such a licence for the trademarks of BT but limited to the Americas (Article 12 (3) (a) and (b)) and vice versa.

The parties have provided the Commission with an array of arguments supporting the indispensability of the exclusive distribution arrangements for BT in the transaction. Both have particularly stressed the protection of the valuable intellectual property rights they have contributed to the joint venture against outsiders but, in particular, against each other. In this context, both parties have stressed that they have not found a more efficient manner of organizing the distribution of the products in a balanced way.

Taking those facts into consideration, together with the high level of competition that the parent companies will be facing (as distributors of Newco) and the substantial bargaining power of customers, the exclusive distribution arrangement for BT (including here those provisions in the IPA that reinforce it) can be accepted as being indispensable to the positive effects (in particular the distribution of the products in an efficient manner) resulting from the restrictive clauses, provided that at least a possibility for passive sales is available for EEA customers. By passive sales is understood, as regards MCI, the possibility offered to a EEA customer of addressing himself to MCI for the provision of Newco products in the EEA with the support of Newco (as regards, for instance, the availability of leased lines or the required customer service) but

without the intervention of BT or with the intervention of BT only as support distributor.

- (60) The Commission has therefore examined the extent to which such passive sales are possible for all kinds of customers. The parties have confirmed that passive sales⁽¹⁾ will be possible irrespective of the actual size and location of customers, and the Commission considers (and the parties have recognized) that passive sales by each distributor to customers in the exclusive territory of the other are indeed a genuine possibility⁽²⁾. Thus, any potential European customer, with activities in at least two Member States, but no presence in the United States of America, can contract with MCI (instead of BT, the exclusive distributor for the EEA) the provision of Newco services in the EEA only. MCI will conclude the sale in America (without infringing any licence granted to it by Newco or any trademark licence granted by BT) and will then ask Newco to procure all necessary use of remote networks (third-party networks) on the most competitive terms available. For so doing, Newco could, in some cases, engage BT's services (in particular as regards regulated services still provided by BT), but will always be obliged to obtain supplies on a competitive basis. In addition, MCI will be responsible for that customer.

In conclusion, the exclusivity is considered indispensable within the meaning of Article 85 (3) of the EC Treaty (and pursuant to Article 53 (3) of the EEA Agreement).

(iii) *MCI's 'loss of rights' pursuant to Article 9 (12) (c) of the IA*

- (61) As explained above, Article 9 (12) (c) of the IA provides for MCI to lose certain rights in the event that MCI becomes engaged in the core business of BT in a territory defined as 'the rest of the world', which includes the entire EEA.

⁽¹⁾ The latest available version of the business plan even makes a distinction between 'remote sales' (where a customer requests a bid from one distributor for services in the other distributor's territory) and 'passive sales' (where a customer requests bids from a distributor which is not responsible for that territory or customer). Both sales can be effected. The relevant distributor will independently prepare a bid without consulting the other, and Newco, to the extent that it will be involved will not disclose to one distributor the prices or conditions it has provided to the other or any confidential information regarding the customer.

⁽²⁾ In addition, differences in MCI and BT prices for Newco services will occur in so far as each will be related to local conditions and supply costs.

- (62) This provision has to be considered against the imbalance between the very high value for each parent company of its proprietary software licensed to Newco (and to each other within their respective territory) and the low level of protection to which the software is entitled under most intellectual property laws in force. Basically, the same software is going to be used by Newco to serve the needs of its international customers and by each parent company to serve the intra-national needs of their customers within their respective territories. In addition, it has to be taken into account that through Newco (and the licences that Newco will grant to its parent companies in respect of any new development) the technologies of both parties will be increasingly interlinked and, hence, will be increasingly difficult to separate.

For these reasons, the parties decided not to include a termination provision in the IPA in case of infringement, and instead to include the 'loss of rights' provisions in the IA. In this respect, the latter can be seen as analogous to the territorial licensor protection permitted under both the patent licensing block exemption regulation (Regulation (EEC) No 2349/84) and the know-how licensing block exemption regulation (Regulation (EEC) No 556/89).

From this point of view, the 'loss of rights' pursuant to Article 9 (12) (c) of the IA are indispensable in particular as a means of permitting confidence between the parent companies to grow and, consequently, to permit the necessary transfer of technology so as to allow Newco to succeed.

- (63) However, as indicated above, such provision will also produce the effect of substantially preventing MCI from entering the EEA using only its own proprietary technology. The Commission sees no justification for accepting this restrictive effect for as long as the agreements are in force.

For that reason, and following discussions with the Commission, the parties have modified the agreements so that the 'loss of rights' provision pursuant to Article 9 (12) (c) of the IA, in so far as the EEA is concerned, will apply only for a period of five years. Once the five-year period in respect of those rights has expired, MCI's 'loss of rights' will be terminated in relation to the EEA.

This five-year period is adequate taking into account that the existing business plan for Newco commits the parent companies for five years and that, in addition, five years is the time required for the set of services to be marketed by Newco to be fully operational.

In view of this modification, the Commission considers that Article 9 (12) (c) of the IA now fulfils the conditions for the granting of an exemption pursuant to both Article 85 (3) of the EC Treaty and Article 53 (3) of the EEA Agreement.

(e) Conclusion

- (64) It is concluded that all the four conditions for the granting of an individual exemption pursuant to Article 85 (3) of the EC Treaty and pursuant to Article 53 (3) of the EEA Agreement in respect of the creation of Newco and in respect of the indispensable restrictions identified above are satisfied.

F. DURATION OF THE EXEMPTIONS

- (65) Pursuant to Article 8 of Regulation No 17, a decision in application of Article 85 (3) of the EC Treaty (and pursuant to Protocol 21 of the EEA Agreement in so far as Article 53 (3) of the EEA Agreement is concerned) shall be issued for a specified period. Pursuant to Article 6 of that Regulation, the date from which such a decision takes effect cannot be earlier than the date of notification. In that respect, in the present case the Decision, in so far as it grants exemption, should take effect:

- from the date the notification was complete, that is from 16 November 1993 to 15 November 2000 as regards the joint venture created between BT and MCI, and the appointment of BT as exclusive distributor of Newco in the EEA,
- as regards the 'loss of rights' for MCI pursuant to Article 9 (12) (c) of the IA, until the end of the fifth year from the date of the adoption of this Decision,

HAS ADOPTED THIS DECISION:

Article 1

On the basis of the facts in its possession, the Commission has no grounds for action pursuant to Article 85 (1) of the EC Treaty and Article 53 (1) of the EEA Agreement in respect of the agreements as notified, relating to the acquisition by BT of a 20 % stake in the sharecapital of MCI, to the appointment of MCI as exclusive distributor of Newco in the Americas pursuant to Article 2 (1) of MCI's Distribution Agreement, to the appointment of BT

as exclusive distributor of Newco in the rest of the world excluding the EEA territory, to MCI's 'loss of rights' pursuant to Article 9 (12) (c) of the Investment Agreement in so far as the territory of the EEA is not concerned, and to BT's 'loss of rights' pursuant to Article 9 (12) (a) of the Investment Agreement.

Article 2

On the basis of the facts in its possession, the Commission has no grounds for action pursuant to Article 85 (1) of the EC Treaty and Article 53 (1) of the EEA Agreement for the duration of the exemption granted to the joint venture in respect of the obligation on BT and on MCI to obtain from Newco all requirements for global products pursuant to Article 3 (1) of each Distribution Agreement and in respect of the non-compete provision as regards the activities of Newco pursuant to Article 18 (1) of the Joint-Venture Agreement.

Article 3

Pursuant to Article 85 (3) of the EC Treaty and Article 53 (3) of the EEA Agreement, the provisions of Article 85 (1) of the EC Treaty and of Article 53 (1) of the EEA Agreement are hereby declared inapplicable for the period from 16 November 1993 to 15 November 2000 to the joint venture, Newco, created between BT and MCI, as notified to the Commission, and to the appointment of BT as the exclusive distributor of Newco within the territory of the

EEA pursuant to Article 2 (1) of BT's Distribution Agreement.

Article 4

Pursuant to Article 85 (3) of the EC Treaty and Article 53 (3) of the EEA Agreement, the provisions of Article 85 (1) of the EC Treaty and of Article 53 (1) of the EEA Agreement are hereby declared inapplicable for a period of five years from the date of the adoption of this Decision to Article 9 (12) (c) of the Investment Agreement.

Article 5

This Decision is addressed to:

British Telecommunications plc,
81 Newgate Street,
UK-London EC1A 7AJ.

MCI Communications Corporation,
1801 Pennsylvania Avenue, NW,
Washington, DC 20006,
USA.

Done at Brussels, 27 July 1994.

For the Commission

Karel VAN MIERT

Member of the Commission