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ROUNDTABLE ON ENSURING ACCESS TO KEY CAPACITY FOR NEW ENTRANTS.

--Hungary--

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The attached document is submitted by the delegation of Hungary to the Working Party No. 2 of the Competition Committee FOR DISCUSSION under Item III of the agenda at its forthcoming meeting on 6 February 2006.

Please contact Mr. Sean Ennis if you have any questions regarding this document [phone number: +33 1 45 24 96 55; Email address: sean.ennis@oecd.org].

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1. CURRENT VIEW OF THE ESSENTIAL FACILITY DOCTRINE WITHIN THE GVH

1. According to the 1984 Competition Act refusal to supply only qualified as an abuse of dominance if the unjustified refusal was repeatedly practiced against the same business partner. In the 1990 and subsequent legislation the refusal did not have to be repeated for the establishment of illegality. This approach in line with the European legislation put more emphasise on the maintenance of the structure of competition.

2. During the early 90's a number of cases were initiated concerning refusal to supply. These procedures mainly affected two sectors, funeral services and waste management. The complaints in the majority of the approximately 30 triggered cases were submitted by undertakings active on the supply side of these services. Their complaints originated in the alleged abuse of the different municipal firms managing cemeteries or waste yards. The existence of dominance was established in all of the cases. Abuses were established in the case of direct refusal to provide access to the facility. On the other hand when access was restricted by the pricing policy of the incumbent illegality was not established. Summing up the lessons of the case law of the early 90's it could be said that the responsibility of a firm enjoying a dominant position built on an essential facility was to be established if:

- The company possessing an essential facility that reasonably can not be acquired or reproduced from other sources,
- Directly hinders its competitor in the use of that facility, provided that
- The parallel use of that facility is possible.

3. Beside ensuring access the GVH concentrated on the conditions for such an access as well. It was clear that equality of arms between the integrated firm and its competitor can only be ensured if the incumbent provides access for itself and its competitor under the same conditions. The determination of the appropriate access price is made uncertain by the need for the establishment of a competitive price level and the level of the deviation from it. Even if the establishment of the competitive price level is possible, the scale of lawful prices is still wide, this envisages the need for a price regulation. According to the GVH the optimal solution would have been the splitting up of the vertically integrated undertaking or if the access price would have been established by the municipality itself.

4. Though a number of cases involved the issue of access to cemeteries and wasteyards as essential facilities the GVH paid no real attention to the elaboration of the concept of essential facilities. Abusive behaviours were analysed within the general framework of refusal to supply. In the analyses more emphasis was put on the establishment of the than existing 30% market share threshold for dominance than on the essential nature of the facility. It can be stated that the fact that the possessed asset qualified as an essential facility caused no alteration in the analysis.

5. Due to new legal provisions providing remedy for the problems and other changes in the legislative background in the mid 90's putting an end to certain legal monopolies cases of different nature were dealt with by the GVH, mainly from the liberalised telecommunications sector. Concerning access to the local loop it was repeatedly established that those infrastructures can not be considered as economically

duplicable, while access to those assets is indispensable to provide a number of services. Nevertheless the essential nature of certain facilities and the impossibility of their duplication only served as a basis for the establishment of dominance neglecting a detailed elaboration of a doctrine on essential facilities.

6. Though the sectors affected by the issue changed during the last fifteen years no appreciable change happened in the approach of the GVH. The doctrine of essential facilities was not elaborated by the Hungarian jurisdiction and it is only considered as a stricter form of dominance, as in the case of the possessed asset duplication is not simply difficult but impossible. Abuses relating to such an asset are therefore covered by the more general approach, namely refusal to supply within which the issue of essential facilities was not distinguished in the jurisdiction.

2. CONTROVERSIAL ISSUES AND DIFFICULTIES REGARDING ACCESS TO ESSENTIAL TRANSPORT INFRASTRUCTURE IN HUNGARY

7. The difficulties and controversial issues which are discussed below has hardly links to substantive debates about the advantages and disadvantages of the existence of access obligations or various access regimes. Instead, they are mostly linked to potential procedural shortcomings and inconsistencies, as well as the institutional background of the regulation.

2.1. Energy

8. Encouraged by the Chairman's letter inviting submissions, this submission deals also with the access to electricity transmission network and cross-border lines since they can be regarded as part of transport facilities in a wider sense. While natural gas storage capacities are not means of natural gas transport in the classical sense, they are complementary elements of the pipelines, and – to some extent – substitute for the pipeline network or for some fractions of the network. As a consequence, natural gas storage facilities constitute a strategic asset, access to which can be equally critical for new entrants as access to the transport infrastructure. Therefore they are also included in this submission.

2.1.1. Access to natural gas storage capacities

9. In Hungary the liberalisation process of the natural gas sector started in 2004. There have been several difficulties in the market opening. One great problem which affects essential facility problem was that the former monopolist MOL Rt. was the owner of the high pressure pipeline company (MOL Földgázszállító Rt.) and (until January, 2006.) it was the owner of gas storage company (MOL Földgáztároló Rt.), and also the owner of the natural gas wholesaler incumbent MOL Földgázellátó Rt. (Hungary adopted the single buyer model).

10. Under the Hungarian natural gas regulation scheme there is regulated TPA to the high pressure and low pressure pipelines, but there is negotiated TPA as regards storage. This inconsistency might allow the incumbent to slow down the potential entrant. This regulation solution is not the only or most important factor of the slow evolution of competition, but an interesting part of the whole picture.

11. Nowadays the ownership structure of natural gas sector is changing; E.on-Ruhrgas International AG acquired the gas wholesaler incumbent (MOL Földgázellátó Rt) and the gas storage company (MOL Földgáztároló Rt) from MOL Rt. The merger had a community dimension and the Commission of the

European Union already adopted its decision about it. In the decision the Commission did not prohibit the merger, but it set up remedies. The potential negative effects of the above mentioned regulation inconsistency was solved by one of the remedies as a side effect; the buyer E.on undertakes to provide the same conditions to its competitors in the gas storage service than to its own wholesaler. This remedy should guarantee that access to storage will not be discriminatory.

2.1.2. Cross-border electricity lines

12. The GVH has drawn up the structure of electricity sector and process of liberalisation in a submission in 2004 (DAFFE/COMP/WP2/WD(2004)50). The transmission grid owner, the TSO monopoly is the state owned MVM Rt. (Magyar Villamos Művek Rt.). Before the liberalisation process begun in 2001, it had strong positions in the wholesale market, in the electricity generation market, in the transmission, import-export of electricity. As a grid owner it has increased responsibility to develop the electricity system. Hungary is a small, open market in respect to the electricity sector. The rate of electricity import is quite high (app. 20%). Hungary has connection points to the neighbouring countries. As a tendency, it can be noticed, that import electricity is much more competitive than the product of domestic power plants, and the domestic generation capacities are bounded by long term power purchasing agreements to MVM. There is a growing demand in developing the high voltage electricity lines, mostly the cross-border lines.

13. System development decisions have several factors; some are professional (system security, ensuring supply of growing electricity demand from import sources, etc.) but some are business in nature, e.g. MVM as system owner has interests in electricity wholesale market (MVM is a public utility wholesaler and MVM is owner of a free market trading company, MVM Partner, which has quite strong position on the electricity free market). MVM is obliged by law to develop the grid, and in theory this development have to serve for the electricity system as a whole. Nevertheless, in practice MVM has a room to manoeuvre, to decide which areas of the grid will be developed. The network which will be built by MVM will be part of the system, and to use this, everybody has to pay system usage fee.

14. In the present stage of liberalisation, some market participants have economic interest to build their own cross-border network and import electricity on this line. The controversy is that regulation can not handle perfectly this intention. It is not clear how to handle this privately owned cross-border lines and this problematic case is in close relation with the problem of access to cross-border transmission capacities, discussed below.

2.1.3. The position of the electricity system operator

15. MAVIR Rt. (Magyar Villamosenergia Rendszerirányító Rt.) is the transmission system operator in Hungary. This firm has the obligation to balance the system, to secure the continuous electricity flow. In 2001. when the liberalisation started, Hungary has chosen the Independent System Operator model. This means that MAVIR Rt. was independent from all market players, it was owned by the state. This independence enabled to bring professional and not by particular interests influenced decisions to the whole electricity sector. The unique solution was that MAVIR was the system operator, but the assets (high voltage networks, secondary reserves, etc.) remained owned by MVM. The decisions brought by MAVIR affected the MVM assets. Several times MAVIR brought decisions which did not favour MVM.

16. The concept of an independent system operator that does not own assets did not prove to be successful. This is why the government decided in 2005 to change the ISO model. Though the GVH suggested that MAVIR should remain independent but that it should own the assets the proposal failed. Based on the decision of the government MAVIR became affiliated to MVM. The ministry of economy argued, that this solution is more optimal than ISO model, the unbundling rules secure the independent

decisions of MAVIR and the TSO model is compatible with the 54/2003 EC Directive. The GVH upholds its opinion that from a competition viewpoint this solution is not perfectly satisfactory.

2.1.4. Auction of cross-border transmission capacities

17. This subject is not a purely domestic issue, therefore cannot be solved solely on the basis of the Hungarian regulation. Domestic power plants do not have sufficient free capacities, so electricity import is an important source for competition in Hungary. Free market players base their supply portfolio mainly on import and as large market players are international energy firms they can import electricity to the Hungarian market from their own power plants in the neighbouring countries.

18. The problem rises from the fact that national regulations set up certain limits to free trading of electricity between states. All states have the responsibility to ensure security of supply in its own country. This requirement means that governments (the Hungarian government also) uphold certain degree of cross-border capacity to unexpected domestic electricity shortage. In addition, there are regulatory differences between the states. Some countries allocate free capacity throughout an auction mechanism, but there are countries, which do not have such competition-based mechanism. The Hungarian regulation regime is different from the Slovakian one as regards the allocation mechanism, but these countries have the right to decide about the 50-50% of the capacity of the connection point. Moreover there are countries (for example Ukraine), which do not have a transparent allocation mechanism.

19. One effect of the differences among the regimes is that a market participant, which has a power plant in a country not too far from Hungary (e.g. in Poland) has to reach coordinated free capacity both on the Poland/Slovakian border, and on the Slovakian/Hungarian border. In the different allocation and regulation regimes this can be hard to execute. In addition, while Hungary has a transparent – although developing – auction mechanism for cross-border capacities, access to these capacities, as a whole, is still not transparent and competition based.

2.2. Railway

20. The controversies described below bear a relation to two different categories of railway infrastructure: on the one hand, deficiencies of the regulatory-prescribed institutional regime of the sector gave reason for concern in case of access to the national public railway network, while on the other hand, unsettled legal and property relations caused difficulties in case of access to certain non-public infrastructure elements.

2.2.1. A brief overview of the Hungarian Railway Sector

21. In the past fifteen years, the direction of regulatory measures taken in the Hungarian railway sector were determined by the developing EU railway directives, due to the obligation of law harmonisation required in the accession process and later as a Member State. During this period, the Hungarian government applied a ‘minimalist’ approach towards the implementation of the EU railway directives, which meant at most the formal obligatory-to-do adoption of the EU regulatory model, and sometimes even an apparently incomplete implementation of the Community legislation.

22. The Railway Act of 1993 and its amendments (1993 Railway Act)¹ gradually implemented the rules for reorganisation of the historical incumbents and the opening of the railway (transport and traction services) markets. On 1st May 2004 the legal framework of liberalisation entered into force, thus rendering

¹ Act XCV of 1993 on Railways

the entrance of new train-operating companies (hereinafter referred to as TOCs) possible. This regulatory framework soon proved to be an insufficient, inconsistent basis for liberalisation.

23. These regulatory shortcomings – as the examples described below might demonstrate – could significantly adjust to the poor achievements characterising the first period of the open market, and resulting that the market structure remained premature and is still dominated by the duopoly structure. By the beginning of 2005, it became clear that regulatory framework had to be taken on new grounds. The new 2005 Railway Act² was finally adopted by Parliament in December and entered into force on 1st January 2006, while the relating government and ministerial decrees – necessary for the proper law enforcement – are still under elaboration. For clarity, it has to be noticed that the access controversies illustrated below related to the regulatory regime existing under the former 1993 Railway Act, as the GVH has no experience concerning the new legislation yet.

24. By the end of 2004, four new TOCs (train operating companies)³ had obtained operating licences beside the two historical incumbents: the Hungarian State Railways Company (hereinafter referred to as „MÁV”) and the Győr-Sopron-Ebenfurt Railway (Ltd.) (“GySEV”)⁴, providing rail freight transport and traction services. The new entrants are privately-owned companies operating with relatively low capital and mostly rented trains and rolling stock, established by freight-forwarders or companies formerly dealing with transport-related rail activities (engineering, track construction).

25. While the duopoly of the two state-owned incumbents cover about 90% and 10%, respectively of the rail freight transport market, and in the first year of liberalisation the CER Co. belonging directly to MÁV has captured about 1 % of the market, the independent companies’ market share amounts to less than 0,1%.⁵

26. In 2003 – in the harmonisation process mentioned above the different core activities of the incumbents were organized into separate business units. These are: (1) Infrastructure management; (2) Passenger transport; (3) Freight transport; (4) Engineering (traction); (5) Real estate management. The functional separation was to enable accounting separation of the different activities, but in its current form

² Act CLXXXIII of 2005 on Railway transport

³ Three of the TOCs are independent companies:

- MMV - Hungarian Private Railways Limited
- Floyd Ltd.
- MÁV Hajdú Construction Ltd. – The company was established in 1992, its main activity is rail track line construction. The MÁV Hajdú Construction Ltd. used to be the subsidiary of MÁV till 2001 June, later it became an independent TOC by obtaining its operating licence in July 2004.

and one tied to MÁV

- "Central-European Railway" Transport, Trading and Service Co. (“CER Co.”). CER Co. was established in October 2004 to offer rail transportation services. According to articles of association the MÁV-REC Co. (subsidiary of MÁV) bears 51 % of the companies share, which means that MÁV has direct control over CER Co.

⁴ GySEV has a special status; it operates a fraction of the Hungarian and the Austrian rail track between Győr (in Hungary) and Ebenfurt (in Austria) under concession and provides passenger and freight transport services.

⁵ Antal, Dániel (2005): The first year of the Hungarian rail freight transport market - A Magyar vasúti áruszállítási piac első éve (Vasútpolitikai konzultációs anyag a magyarországi áruszállítási piac első évének tapasztalatairól) Available only in Hungarian.

it proved to be insufficient to meet the requirements of the transparent and fair operation of the integrated railway companies on the liberalized market.

2.2.2. Access to the national public railway network

27. The 1993 Railway Act categorises the Hungarian railway infrastructure (i.e. the railway network and its accessories) by the owner: most of the railway lines are owned exclusively by the state (national network) or municipalities (local networks) and can be used publicly, and on the other hand there are privately-owned and used railway tracks. The national public railway network is operated by the infrastructure management divisions of the incumbents, and is used for all kinds of freight and passenger transport services.

28. The Act and the relating ministerial decrees specified the access regime of the national public railway network. Under this regime, train paths concerning railway lines belonging to the national public network are allocated by the Vasúti Pályakapacitás-elosztó Kft. (hereinafter referred to as VPE). VPE is the capacity allocation and charging body required by EU law. This institution is state-owned and independent of any railway companies. Concerning its legal form, VPE is a commercial entity, but the capacity allocation process made by VPE constitutes an administrative procedure under the 1993 Railway Act. Briefly, VPE is responsible for developing and publishing the capacity allocation and charging framework in the Network Statement, and deciding on concrete capacity allocation requests filed in according to the Network Statement. The Network Statement includes detailed data on line capacity, conditions of entering lines, restrictions of track usage as well as rules of procedure and charging scheme.

29. For reasons inherent in the system itself, VPE needs active contribution of the infrastructure management division of the vertically-integrated incumbent in question when trying to complete its tasks. This simply derives from the fact that it is the infrastructure manager who is in possession of information (e.g. on technology and traffic) and systems to produce the information as well. Therefore, when drawing the Network Statement or deciding on a capacity request, VPE cannot avoid consultation with the relevant infrastructure manager. In practice, lack of administrative and technical capacities resulted that in majority of cases VPE had no other choice but to rely almost completely on data provided by the incumbent, as it had not been in a position to at least check the information submitted by the incumbent, thus to provide (regulatory) oversight over the allocation process and its outcome.

30. Moreover, in spite of the fact that the decision of VPE and the allocated train path defined therein constitutes a right to access, it does not in itself allow for track use. The TOC is obliged to conclude an access contract with the infrastructure manager, defining the concrete terms of track use on the basis of the Network Statement and the VPE decision. The position of the parties is certainly not equal when concluding the access contract and negotiating on its terms, and neither VPE, nor any (other) railway authority had supervisory competences in this second part of the capacity allocation process.

31. Above all, the so-called Pályahasználati Testület (hereinafter referred to as PT), which was dedicated to fulfil the functions of the regulatory body of the sector under the 1993 Railway Act, had never been set up actually. It should have been a body operating besides the Supreme Transport Authority and deciding on appeals against the measures of VPE, while it lacked any other regulatory competences. In many controversial cases the absence of PT resulted that VPE had to play a mediatory role between the relevant parties without legal mandate.

32. Though “de iure” even two institutions were established to guarantee the fair and non-discriminatory treatment of new entrants when applying for access to the national public railway network, the circumstances described above all adjusted to the unchanged decisive role of the incumbents in the capacity allocation process.

2.2.3. Access to certain non-public infrastructure elements

33. Access is crucial for new entry also to infrastructure elements such as certain tracks (used for e.g. loading, unloading or re-loading wagons, for repairing trains), certain station facilities. Most of these infrastructure elements as well as tracks connecting the premises of industrial customers with the public railway networks are non public and do not belong to the national or local public network (these elements hereinafter referred to as industrial railway lines or feeder lines).

34. In Hungary, new entrants faced difficulties in accessing industrial lines managed or owned by the incumbent MÁV. Carriage of bulk goods constitutes – in respect of stability, competitiveness and profitability of railway sector – the most important segment of the Hungarian rail freight transport market, where house-to-house transport service is the only plausible option. For this reason, it is essential to have access to the feeder line serving logistic purposes for the customer. It is estimated that 70-75 % of the freight transport turnover in Hungary is realised with the use of these privately-owned industrial railway tracks, and MÁV – exclusively or partially – owns or manages majority of industrial lines of bulk goods shippers like power plants, mines, sugar works, cement works, mills etc. In this respect, the feeder lines are playing a role in the case of this kind of customers that is similar to the function of ‘last mile’ or ‘local loop’ in telecommunications, i.e. these are the end points to network at the customer.

35. The access controversies concerning MÁV-owned industrial lines resulted from the unsettled legal and property relations of these lines.

36. According to the 1993 Railway Act the national public railway networks and the local public railway networks are exclusively owned by the state and municipalities respectively, while non-public railway infrastructure can be owned by any natural or legal entity. The unsettled property status of feeder lines has historical roots. Most of these industrial lines were built decades ago either by the state-owned incumbent railway company or by the similarly state-owned industrial customer, the so-called industrial track user. In the 1950’s MÁV was statutory obliged to take over maintenance and operation of industrial lines, and in many cases the licences of the industrial tracks were also transferred to MÁV. After a while, this resulted quasi-proprietary rights to MÁV.

37. As a result, some of the Hungarian industrial railway tracks are owned by the industrial customers, some of them by the incumbent railways, and sometimes the property relations are mixed: some of the assets of the track belong to the incumbent railway company and some of its other assets to the industrial rail track user, but all of them may qualify as non-public infrastructure elements. As we mentioned above, the exclusively or at least partially MÁV-owned industrial lines constitute the majority both in number and importance.⁶ What is more, the management and operation of MÁV-owned industrial lines – contrary to the national public network – belonged not to the infrastructure management, but the cargo division of MÁV. Both the MÁV and the regulator treated the management of industrial lines a cargo-related activity when the ministerial decree on the unbundled accounting of railways activities had prescribed the management of this infrastructure as task of the cargo division. Consequently, other TOCs (the new entrants) had to turn to MÁV cargo division, their direct competitor, for accessing industrial lines.

38. The freight service provision and the handling of goods – guided by contracts – on the industrial track exist independent of property relations, and these contractual relations between the service-provider railway companies and the industrial track users make the accessing possibilities even more complicated.

⁶ In case the industrial rail track belongs – at least partially – to the railway company, first of all the railway company and the industrial customer conclude a hire contract on the use of the track for rail freight operation purposes by the customer against a fee.

39. In close connection with the unsettled property relations, the unclear legal status of these infrastructure elements could also adjust to different interpretation of laws. On the one hand, a provision of the 1993 Railway Act can be interpreted as an obligation of the incumbent to grant access to any infrastructure elements irrespectively whether they belong to the public or non-public infrastructure. On the other hand however, the relevant EU legislation⁷ as well as the 1993 Railway Act provides for the special treatment of certain privately owned infrastructure elements, moreover the incoherent terminology used in the relevant pieces of Hungarian railway regulation and the absence of clearly defined distinction between public and private lines – both in regulation and in the Network Statement – lead to the situation where the operational and specified regulatory framework covers only access to the national public infrastructure. In spite of the alleged access obligation to the rest of the infrastructure owned by MÁV, there is no practical procedural opportunity to realise such an obligation (e.g. VPE's competence covers only issues regarding the national public railway infrastructure).

40. As accessing industrial lines play an important role for rail freight transport service-providers, the controversies described above were brought to light in a few months after market-opening. MÁV first completely refused, then considerably hindered new entrants to access these lines, but later changed its point of view and made the access possible for competitors as well – though the access regime worked out by MÁV for industrial lines and other non-public infrastructure elements were sometimes also criticised by the new TOCs. The proprietary and contractual rights of MÁV relating to certain infrastructure elements in the unclear regulatory background were sufficient for MÁV to solely control accessing – in fact, sometimes the inadequate regulatory measures themselves promoted or justified the behaviour of MÁV.

41. The new entrants turned to all possible forums including the competition authority to complain about the 'refusal to access' practice of MÁV and seek for remedy. The GVH initiated proceedings against MÁV to investigate whether the incumbent's behaviour infringed the Competition Act.

2.2.4. Recent developments that might resolve controversial issues in access to railway infrastructure

42. As it is noticed in the introduction, the new 2005 Railway Act has just entered into force on 1st January 2006. The 2005 Railway Act has established the Hungarian Railway Office, redefines certain ambiguous categories and reforms rules governing access and operating licensing to a substantial extent.

43. On 9 September 2005 the Government decided to divide the MÁV freight transport activity into a separate company. The MÁV Cargo Ltd. was registered in November 2005 and it has begun its commercial operation on 1st of January 2006. The MÁV Cargo Ltd. is the subsidiary of the MÁV, although and MÁV has direct control over it. MÁV has decided that no 'industrial' rail track would be owned or operated by the MÁV Cargo. The 'industrial' rail tracks will be owned by MÁV and operated by MÁV's Infrastructure management division.

⁷ Directive 2001/14/EC – on the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure and safety certification – Article 1. 3 (d)