**UNITED KINGDOM**

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# RESPONSE TO THE PUBLIC CONSULTATION ON A DRAFT COMMISSION RECOMMENDATION ON RELEVANT MARKETS*

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* Relevant Product and Service Markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communication networks and services


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**UK Response to Commission Communication on the Recommendation on relevant markets for electronic communications networks and services**

## 1 Introduction

This response reflects the position of the UK Government and the independent UK communications regulator, Ofcom. We have also responded, in a separate paper, to the Commission's Communication on the Review of the Regulatory Framework for electronic communications networks and services.

### 1.1 Executive Summary

It is clear that the introduction of the Framework in 2003 has contributed to a significant improvement in the competitiveness and openness of European electronic communications markets. However, this has not occurred at the same rate or to the same extent across the EU, and real differences remain. While the UK has been able to remove retail regulation from the markets proposed to be deleted from the Recommendation on relevant markets, there are still Member States which have yet to complete their first round of market reviews. It is therefore probably not appropriate to reduce the list at the present time. At the same time, the UK would like to emphasise the importance of the need for NRAs to have the flexibility to define (and regulate, as appropriate) markets (including new markets, whether converged or "emerging") as and when national market conditions dictate.

The UK has also taken this opportunity to address the following issues:

- NRAs' ability to impose regulation in adjacent retail markets in support of remedies at the wholesale level, where necessary to ensure regulation is fully effective. In particular, the UK argues that competition law does not always successfully address cross-market leveraging, and would welcome the explicit recognition that a range of ex ante instruments may be suitable to deal with this;
- the inability of the *AirTours* test to address certain forms of collective dominance;
- the application of the three criteria. In particular the UK argues for the alignment of the timescales in the first and second criteria;
- the need to consider indirect constraints as part of the SMP analysis, rather than when defining the market, consistent with European jurisprudence;
- the need to differentiate between captive and non-captive self-supply, and the dangers in presuming that self-supply by the incumbent should always be considered in calculating market shares (and similarly that self-supply by alternative operators should never be considered); and
- the need to consider transitional provisions carefully so as not to risk causing the unnecessary expending of regulatory resource.

## 2 Market definition, identifying markets and definition of other markets

### 2.1 Three criteria

The UK notes that the three criteria are essentially a screening device, ensuring that all NRAs assess the potential for ex-ante regulation in specific sectors based on a common systematic approach, and using the same criteria. Meeting the three criteria simply permits a more detailed consideration of the issues to be carried out in a market review, which in turn determines whether or not regulation is necessary.

In this context, we note the Commission's assertion that, in applying the second criterion (no tendency towards effective competition), NRAs need only find "clear evidence of dynamics in the market within the period of the review which indicates that the market will reach the status of effective competition in the longer-run without ex ante regulation in the market concerned". If evidence of projected effective competition *beyond* the period of the market review is found, then the second criterion is not met, and a market review is not required.

The UK believes that, while in some cases it may not be appropriate to regulate a market which is expected to become effectively competitive in the medium term (i.e. *beyond* the period of the market review), this conclusion should be reached only following a detailed examination of the market in question, rather than the less detailed analysis of the three criteria. NRAs should be able to consider whether or not it is appropriate to regulate prospectively competitive services on a case-by-case basis. It may, for instance, be appropriate to impose some form of light touch regulation to protect consumers during the period of the market review, even if effective competition is anticipated after the period of the market review. Otherwise, NRAs could be prevented from fulfilling their duty of protection of citizens under Article 8 of the Framework Directive.

Aligning the timescales in the second criterion and market reviews would not necessarily result in a greater degree of regulation. Indeed, a market review might result in an SMP finding, but nonetheless conclude that the imposition of minimal remedies only is appropriate, given the timescale of the anticipated effective competition. In addition, aligning the timescales will provide greater regulatory certainty to stakeholders and facilitate the consistent application of the second criterion by NRAs across Europe.

Furthermore, if the timescale of the second criterion and the market review are not aligned, then this could introduce an inconsistency between the outcomes of the three criteria test and the SMP analysis. It could be the case that the three criteria test suggests that a market is not susceptible to ex ante regulation because in the longer term (i.e. beyond the period of the market review) the market tends to competition. This could be in direct contradiction to an SMP analysis of the same market, which could find that, during the period covered by the market review, the undertaking has SMP and therefore that some form of regulation (however light) may be appropriate. This conceptual inconsistency suggests that the two timescales should be aligned.

### 2.2 LLU & WBA, Cable & DSL

The Commission states categorically that wholesale unbundled access to metallic loops and wholesale broadband access (WBA) are separate markets. While the UK currently defines them as separate markets, as copper is progressively replaced by fibre in the access networks there will be a strong argument for defining them in a technologically neutral way, and it is possible therefore that they will not be separate markets. We would therefore expect the revised Recommendation to reflect this dynamic.

The Commission also argues that cable and DSL are always separate markets, and that indirect constraints should be considered as part of the SMP analysis (rather than when defining the market). The UK believes that indirect constraints should be considered as part of the market definition, and indeed the Court of First Instance has consistently stated that indirect constraints can be used not only at the market power assessment stage, but also in the market definition stage, i.e., to establish whether different upstream goods belong to the same market even if they are not directly substitutable. The revised Recommendation should be consistent with this jurisprudence.

### 2.3 Remedies - Leveraging

The UK welcomes the Commission's statement that, as a consequence of an SMP finding, NRAs may impose obligations in areas outside, but closely related, to the relevant SMP market under review (subject to the criteria of appropriateness, proportionality, efficiency), and as long as these obligations are essential to ensuring the effectiveness of the remedy in the SMP market. The UK notes the Commission's example of accounting separation, which is well-established, but the UK believes that other types of remedy may also need to be considered in these circumstances, as necessary (subject always to those criteria). Accordingly, to clarify the position, it urges the Commission to deploy a wider range of examples in its guidance.

Appropriate examples may include publication or notification requirements relating to services in the adjacent market, the specification of a minimum margin between the price of services in the SMP market and the corresponding price of services in a downstream market, or other measures aimed at preventing the circumvention of wholesale remedies through commercial policies in retail markets. As discussed in the ERG Common Position on Remedies, without such remedies, the traditional remedies imposed on services in the SMP market (such as non-discrimination) may in particular circumstances be ineffective. Indeed, wholesale remedies may create incentives on operators to act anti-competitively in a downstream market, thus undermining the effectiveness of the upstream remedy, and creating conditions in the downstream market that are less than effectively competitive.

The Commission asserts that competition law provides the appropriate instruments to deal with market failures in non-SMP markets caused by the use of commercial strategies (such as price squeeze) by operators who are dominant in adjacent markets. This may not be true in all circumstances and cases of leveraging do arise in practice which produce detrimental effects on competition and consumer choice in an adjacent market, but which may not necessarily amount to an abuse of a dominant position. For instance, a dominant operator which is more efficient, for example due to significant economies of scale and/or scope (and consequently low marginal costs), may be able to price competitors out of an adjacent market (where it does not necessarily have dominance) and this may not be considered an abuse of its dominant position. In addition, an NRA may wish to prevent such leveraging in order to fulfil an Article 8 duty where such duty may not be relevant to the application of competition law, for example, to encourage market entry or investment in infrastructure, even if prices could (in the short term, at least) increase as a result. In other words, the beneficial dynamic effects of regulatory intervention (increased competition, innovation, consumer choice) could outweigh the negative static effects (higher prices). The UK would therefore propose a less absolute statement from the Commission that recognises the suitability of ex ante instruments in particular circumstances, of course always subject to the principles of appropriateness, proportionality and efficiency, and as long as these ex ante remedies are necessary.

### 2.4 Collective dominance

As noted in our response to the Commission's Call for Input, the Framework does not currently provide the tools needed to deal with certain types of oligopolistic markets that are less than effectively competitive. We note, however, that the Commission has not made any proposals in relation to the SMP Guidelines, where the guidance on assessing collective dominance in oligopolistic markets is set out (by reference to the judgment of the Court of First Instance in *AirTours*). A more detailed discussion of this point appears in our response to the Communication on the review of the Regulatory Framework.

## 3 General Issues

### 3.1 Self-supply

The Commission does not differentiate between self-supply that is captive (i.e. cannot be diverted to the merchant market during the period relevant for the definition of the relevant market, and therefore should be excluded from the market definition) and self-supply that is not captive (can be diverted, therefore should be included in market definition). Indeed, the Commission appears to presume that all self-supply (by the incumbent) is always captive (and is therefore to be excluded from the market definition). We believe this is an empirical matter that needs to be assessed and determined on a case-by-case basis. Indeed, European case precedent reveals that both the CFI and the Commission have also recognised the need for case-by-case analyses to determine whether some internal transactions (self-supply) or some sales under long-term or relational contracts should be considered effectively "captive".

It would be preferable if the Commission expressed its guidance through a statement of principles rather than only by way of examples (though examples can be useful to illustrate the principles). For example, the Commission appears to presume that "alternative firms" will be capacity-constrained. While this is a relevant consideration in determining whether or not the internal supply of alternative firms is captive, it should not be presumed. In the absence of general statements of principle, there is a danger that NRAs will interpret the Commission's guidance as establishing (for instance) the (incorrect) principle that self-supply by the incumbent should *always* be taken into account, while self-supply by other operators should *not* be taken into account when calculating market shares. The assumption that all cases in the communications industries will exhibit the same empirical characteristics can lead to incorrect outcomes.

### 3.2 Converged markets, bundling

The Commission considers that converged offerings between mobile and fixed services may emerge in the future, but that this is not expected to be a widespread phenomenon during the life of the revised Recommendation. Furthermore, it believes there is little evidence to consider triple or quadruple plays as a bundle that should be analysed as a single market.

The UK believes that market definitions will need to evolve in line with convergence and technological development, and that this process is likely to take place at different rates across Member States. On that basis, the UK accepts that converged markets may not need to be analysed yet, and that triple or quadruple bundles may not yet be considered a single market. However, the UK believes that this approach should not prevent NRAs from defining and appropriately regulating markets as they consider it appropriate based on national circumstances, and therefore urges the

Commission to ensure that the revised Recommendation expressly reflects (through specific wording) NRAs' flexibility in this respect.

### 3.3 Emerging markets, Next Generation Networks (NGNs)

The UK agrees with the Commission that that evolution will not proceed at a uniform rate across the EU and there may well be increased heterogeneity. We therefore believe NRAs will require flexibility to take this into account when defining markets and setting appropriate remedies. The revised Recommendation should reflect NRAs' flexibility in identifying economic markets which are appropriate to the national state of evolution, not based on the state of the fastest- or slowest-evolving market or on some advance expectation of a European norm.

However, we do not believe that the concept of "emerging markets" adds anything useful to the combination of (a) the three criteria, and (b) the principle of proportionality in the choice of remedies. We would welcome the amendment of the text to reflect the need for NRAs to retain flexibility in this respect.

We also recognise that it is important to provide regulatory certainty to investors, particular in the case of risky bottlenecks. In particular, where Next Generation Access is used to deliver services which are completely novel, they should be regulated in a manner which recognises the demand-side risk (i.e. uncertain revenues) associated with such services. However we are opposed to regulatory holidays because returns on such investments will be made only over long periods, and a 3-5 year regulatory holiday would do no more than provide a barrier to entry to rival, competitive investment. In short, regulatory holidays will tend to cause more problems than they seek to solve by delaying the imposition of effective remedies. Instead, appropriate remedies should be imposed at the earliest (appropriate) opportunity.

## 4 Examination of markets to identify relevant markets for the purposes of the recommendation

### 4.1 Removal of retail markets 3-6 (4.1)

We agree with the Commission's aim of reducing regulatory burdens at the earliest appropriate opportunity. Clearly, where effective wholesale remedies are in place, there should be scope for the removal of downstream, retail regulation The UK has dealt with enduring SMP issues in the fixed wholesale market, allowing Ofcom to remove certain retail regulations from BT. This has shown that once regulation is effective at the wholesale level, the risks associated with removing retail regulation dramatically reduce. However, the Commission has not provided sufficient evidence that competitive conditions across the majority of the 25 EU Member States warrants the removal of these markets from the list of relevant markets. Considering this, and given late transposition of the Framework in some countries (and in particular the fact that not all regulators have completed all market reviews), it may be appropriate to retain retail markets on the list for a further, transitional, period.

We would therefore support retaining the current list, with another review of the Recommendation in two years' time (before the amended Framework comes into effect in 2009/10), when there may be a better case for the removal of retail markets. Furthermore, we would recommend that markets are not removed in a particular Member State until a first market review has been completed

In any event, it is imperative that Member States which have already found markets to be competitive should not be required to carry out further reviews of those markets even if they remain on the list. The UK therefore welcomes the Commission's clarification to this effect in Recital 16 of the draft revised Recommendation.

Furthemore, the deletion or retention of these retail markets should not affect NRAs' ability (when regulating the related wholesale markets), to apply safeguard/detection remedies in adjacent retail markets without the need for such retail markets to be defined and subjected to a market review (this is further discussed in paragraph 2.3 above.

### 4.2 Inclusion of SMS in mobile voice termination market (4.2.4)

The UK considers SMS to be in a separate market to mobile voice termination in the UK, and one that should be reviewed. Should the two markets be combined in the final Recommendation, NRAs should nonetheless consider the two markets separately where national circumstances justify this approach, and the UK welcomes the Commission's express acknowledgement that NRAs may treat them separately.

### 4.3 Market 15 - wholesale mobile access and call origination (4.2.1)

This market has been found to be effectively competitive in the UK, and therefore we see no need for a review of that position at present. However, we are not aware that this is the case across the EU, and indeed there may be a need in the UK for a future review in the event of changed circumstances. It may therefore be appropriate to retain the market on the list of relevant markets. In the meantime we believe that there should be no obligation for NRAs to review any market where that market has already been found to be competitive, whether or not it is kept on the list. In this respect, we welcome the express language in the draft Recommendation indicating that NRAs may choose not to review a market which is on the list, but which does not pass the three criteria (which competitive markets would not).

### 4.4 Market 18 - broadcasting transmission (4.2.5)

The UK believes that it is very likely that most, if not all, NRAs will continue to be able to define a broadcasting transmission market satisfying the three Criteria for some time to come. On the basis of experience to date, it will be a segment of the market defined by the Commission and, moreover, the segments will vary considerably across Europe. In the UK, for example, one of the key considerations governing market definition is the requirement in their licences for public service broadcasters to broadcast via the terrestrial transmission network. This gives rise to entrenched market power enjoyed by the owners of terrestrial transmission sites. However, this may be an irrelevant consideration in other Member States, for example those where most consumers rely on cable or satellite transmission.

On this basis, broadcasting transmission will be an area worthy of regulatory attention for some time to come. Notwithstanding the considerable variation in market definition, it would be very odd if the area did not continue to be covered by the Commission Recommendation.

## 5 Transition to the new recommendation and subsequent revision

We believe that NRAs which have just finished their market analyses before any new Recommendation comes into force should not be expected to start new market analyses earlier than after the usual review period. This should be taken into account in the wording of Article 16 of the Framework Directive. In particular, NRAs should be able to prioritise their market reviews to determine the appropriate time to begin a review given regulation already in place and based on national circumstances. For instance, if a market is currently regulated through a 4-year charge control, it may be premature to revisit it any earlier, regardless of the updating of the Recommendation. In such cases a premature market analysis would simply result in the inefficient expending of (scarce) regulatory resources.