

## EFTA SURVEILLANCE AUTHORITY RECOMMENDATION

of 5 November 2008

**on relevant product and service markets within the electronic communications sector susceptible to *ex ante* regulation in accordance with the Act referred to at point 5cl of Annex XI to the EEA Agreement (Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communication networks and services), as adapted by Protocol 1 thereto and by the sectoral adaptations contained in Annex XI to that Agreement**

(2009/C 156/12)

THE EFTA SURVEILLANCE AUTHORITY,

States adopt a recommendation on relevant product and service markets.

HAVING REGARD to the Agreement on the European Economic Area <sup>(1)</sup>,

HAVING REGARD to the Agreement between the EFTA States on the establishment of a Surveillance Authority and a Court of Justice, and in particular Article 5(2)(b) thereof,

HAVING REGARD to the Act referred to at point 5cl of Annex XI to the EEA Agreement (Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communication networks and services) <sup>(2)</sup>, as adapted by Protocol 1 thereto and by the sectoral adaptations contained in Annex XI to that Agreement, and in particular Article 15 thereof,HAVING REGARD to the Authority's Decision No 194/04/COL of 14 July 2004 adopting a Recommendation on relevant markets within the electronic communications sector susceptible to *ex ante* regulation and Guidelines on market analysis and assessment of significant market power,

Whereas:

- (1) The Framework Directive establishes a legislative framework for the electronic communications sector that seeks to respond to convergence trends by covering all electronic communications networks and services within its scope. The aim of the regulatory framework is to reduce *ex ante* sector-specific rules progressively as competition in the market develops.
- (2) Article 15 of the Framework Directive provides that the EFTA Surveillance Authority (hereinafter the Authority) shall, after public consultation and consultation with national regulatory authorities (NRAs) in the EFTA

- (3) The purpose of this Recommendation is to identify those product and service markets in which *ex ante* regulation may be warranted in accordance with Article 15(1) of the Framework Directive. The objective of any *ex ante* regulatory intervention is ultimately to produce benefits for end-users by making retail markets competitive on a sustainable basis. The definition of relevant markets may and does change over time as the characteristics of products and services evolve and the possibilities for demand and supply substitution change. As the Recommendation of 14 July 2004 <sup>(3)</sup> has been in force for more than four years, it is now appropriate to revise it on the basis of market developments in the EEA. Hence, this Recommendation replaces the Recommendation of 14 July 2004, as adopted by Decision No 194/04/COL.
- (4) Article 15(1) of the Framework Directive requires the Authority to define markets in accordance with the principles of competition law. Competition law principles are therefore used in this Recommendation to set product market boundaries within the electronic communications sector, while the identification or selection of defined markets for *ex ante* regulation depends on those markets having characteristics which may be such as to justify the imposition of *ex ante* regulatory obligations. The terminology used in this Recommendation is based on terminology used in the Framework Directive and Directive 2002/22/EC <sup>(4)</sup>. In accordance with the Framework Directive, it is for national regulatory authorities to define relevant markets appropriate to national circumstances, in particular relevant geographic markets within their territory.

<sup>(1)</sup> Hereinafter referred to as the 'EEA Agreement'.

<sup>(2)</sup> OJ L 108, 24.4.2002, p. 33. Directive as amended by Regulation (EC) No 717/2007 (OJ L 171, 29.6.2007, p. 32). Hereinafter referred to as the 'Framework Directive'.

<sup>(3)</sup> EFTA Surveillance Authority Recommendation of 14 July 2004 on 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, as incorporated into the Agreement on the European Economic Area (OJ L 113, 27.4.2006, p. 18 and EEA Supplement No 21, 27.4.2006, p. 33). Adopted by Decision No 194/04/COL.

<sup>(4)</sup> Directive of the European Parliament and of the Council of 7 March 2002 on universal service and users rights relating to electronic communications networks and services (Universal Service Directive), (OJ L 108, 24.4.2002, p. 51, as inserted to point 5 cm of Annex XI to the EEA Agreement by Joint Committee Decision No 11/2004 (OJ L 116, 22.4.2004, p. 60 and EEA Supplement No 20, 22.4.2004, p. 14).

- (5) The starting point for the identification of markets in the Recommendation is the definition of retail markets from a forward-looking perspective, taking into account demand-side and supply-side substitutability. Having defined retail markets, it is then appropriate to identify relevant wholesale markets. If the downstream market is to a large extent supplied by a vertically-integrated undertaking or undertakings, it might be difficult for potential non-integrated undertakings to obtain the necessary input. Consequently, in order to determine whether the market is susceptible to *ex ante* regulation, it may be necessary to construct a theoretical upstream wholesale market. Markets in the electronic communications sector are often of a two-sided nature, in that they comprise services provided over networks or platforms that bring together users on either side of the market; for example end-users that exchange communications, or senders and receivers of information or content. These aspects need to be taken into account when considering the identification and definition of markets, as they can affect both the way markets are defined and whether they have the characteristics which may justify the imposition of *ex ante* regulatory obligations.
- (6) In order to identify markets that are susceptible to *ex ante* regulation, it is appropriate to apply the following cumulative criteria. The first criterion is the presence of high and non-transitory barriers to entry. These may be of a structural, legal or regulatory nature. However, given the dynamic character and functioning of electronic communications markets, possibilities to overcome barriers to entry within the relevant time horizon should also be taken into consideration when carrying out a prospective analysis to identify the relevant markets for possible *ex ante* regulation. Therefore the second criterion admits only those markets whose structure does not tend towards effective competition within the relevant time horizon. The application of this criterion involves examining the state of competition behind the barriers to entry. The third criterion is that application of competition law alone would not adequately address the market failure(s) concerned.
- (7) The main indicators to be considered when assessing the first and second criteria are similar to those examined as part of a forward-looking market analysis, in particular, indicators of barriers to entry in the absence of regulation, (including the extent of sunk costs), market structure, market performance and market dynamics, including indicators such as market shares and trends, market prices and trends, and the extent and coverage of competing networks or infrastructures. Any market which satisfies the three criteria in the absence of *ex ante* regulation is susceptible to *ex ante* regulation.
- (8) From a competition point of view, newly emerging markets should not be subject to inappropriate obligations, even if there is a first mover advantage, in accordance with the Framework Directive. Newly emerging markets are considered to comprise products or services, where, due to their novelty, it is very difficult to predict demand conditions or market entry and supply conditions, and consequently difficult to apply the three criteria. The purpose of not subjecting newly emerging markets to regulatory measures in the name of competition is to promote innovation as required by Article 8 of the Framework Directive; at the same time, foreclosure of such markets by a leading undertaking should be prevented, as also indicated in the Authority's guidelines on market analysis and the assessment of significant market power under the regulatory framework for electronic communications and services<sup>(1)</sup>. Incremental upgrades to existing network infrastructure rarely lead to a new or emerging market. The lack of substitutability of a product has to be established from both demand and supply-side perspectives before it can be concluded that it is not part of an already existing market. The emergence of new retail services may give rise to a new derived wholesale market to the extent that such retail services cannot be provided using existing wholesale products.
- (9) As far as barriers to entry are concerned, two types are relevant for the purpose of this Recommendation: structural barriers and legal or regulatory barriers.
- (10) Structural barriers to entry result from original cost or demand conditions that create asymmetric conditions between incumbents and new entrants impeding or preventing market entry of the latter. For instance, high structural barriers may be found to exist when the market is characterised by absolute cost advantages, substantial economies of scale and/or economies of scope, capacity constraints and high sunk costs. To date, such barriers can still be identified with respect to the widespread deployment and/or provision of local access networks to fixed locations. A related structural barrier can also exist where the provision of service requires a network component that cannot be technically duplicated or only duplicated at a cost that makes it uneconomic for competitors.
- (11) Legal or regulatory barriers are not based on economic conditions, but result from legislative, administrative or other state measures that have a direct effect on the conditions of entry and/or the positioning of operators on the relevant market. An example of a legal or

<sup>(1)</sup> EFTA Surveillance Authority Guidelines of 14 July 2004 on market analysis and the assessment of significant market power under the regulatory framework for electronic communications networks and services referred to in Annex XI of the Agreement on the European Economic Area (OJ C 101, 27.4.2006, p. 1 and EEA Supplement No 21, 27.4.2006, p. 1).

regulatory barrier preventing entry into a market is a limit on the number of undertakings that have access to spectrum for the provision of underlying services. Other examples of legal or regulatory barriers are price controls or other price-related measures imposed on undertakings, which affect not only entry but also the positioning of undertakings on the market. Legal or regulatory barriers, which can be removed within the relevant time horizon, should not normally be deemed to constitute an economic barrier to entry, such as to fulfil the first criterion.

- (12) Barriers to entry may also become less relevant with regard to innovation-driven markets characterised by ongoing technological progress. In such markets, competitive constraints often come from innovative threats from potential competitors that are not currently in the market. In innovation-driven markets, dynamic or longer-term competition can take place among firms that are not necessarily competitors in an existing 'static' market. This Recommendation does not identify markets where barriers to entry are not expected to persist over a foreseeable period. In assessing whether barriers to entry are likely to persist in the absence of regulation, it is necessary to examine whether the industry has experienced frequent and successful entry and whether entry has been or is likely in the future to be sufficiently immediate and persistent to limit market power. The relevance of barriers to entry will depend inter alia on the minimum efficient scale of output and the costs which are sunk.
- (13) Even when a market is characterised by high barriers to entry, other structural factors in that market may mean that the market tends towards an effectively competitive outcome within the relevant time horizon. Market dynamics may for instance be caused by technological developments, or by the convergence of products and markets which may give rise to competitive constraints being exercised between operators active in distinct product markets. This may also be the case in markets with a limited — but sufficient — number of undertakings having diverging cost structures and facing price-elastic market demand. There may also be excess capacity in a market that would normally allow rival firms to expand output very rapidly in response to any price increase. In such markets, market shares may change over time and/or falling prices may be observed. Where market dynamics are changing rapidly, care should be taken in choosing the relevant time horizon so as to reflect the pertinent market developments.
- (14) The decision to identify a market as susceptible to *ex ante* regulation should also depend on an assessment of the sufficiency of competition law to address the market failures that result from the first two criteria being met.

Competition law interventions are unlikely to be sufficient where the compliance requirements of an intervention to redress a market failure are extensive or where frequent and/or timely intervention is indispensable.

- (15) The application of the three criteria should limit the number of markets within the electronic communications sector where *ex ante* regulatory obligations are imposed and thereby contribute to the aim of the regulatory framework to reduce *ex ante* sector-specific rules progressively as competition in the markets develops. These criteria should be applied cumulatively, so that failure to meet any one of them would indicate that a market should not be identified as susceptible to *ex ante* regulation.
- (16) Regulatory controls on retail services should only be imposed where national regulatory authorities consider that relevant wholesale measures or measures regarding carrier selection or pre-selection would fail to achieve the objective of ensuring effective competition and the fulfilment of public interest objectives. By intervening at the wholesale level, including with remedies which may affect retail markets, EEA States can ensure that as much of the value chain is open to the normal competitive process as possible, thereby delivering the best outcomes for end-users. This Recommendation therefore mainly identifies wholesale markets, the appropriate regulation of which is intended to address a lack of effective competition that is manifest on end-user markets. Should a national regulatory authority demonstrate that wholesale interventions have been unsuccessful, the relevant retail market may be susceptible to *ex ante* regulation provided that the three criteria set out above are met.
- (17) On 17 December 2007, the European Commission issued a new Recommendation 2007/879/EC<sup>(1)</sup> on relevant product and service markets within the electronic communications sector susceptible to *ex ante* regulation in accordance with the Framework Directive.
- (18) The starting point for the revision of the Authority's Recommendation on relevant markets is the Commission's new Recommendation and the considerations of the Commission in the Explanatory Note to its Recommendation. In its revision process, the Authority has taken the approach that the comparison of market developments should be carried out against an EEA benchmark and not just taking into account the market situation within the individual EFTA States.

(<sup>1</sup>) OJ L 344, 28.12.2007, p. 65.

- (19) On the basis of market developments in the EFTA States as well as comments submitted in the public consultation and other information available to the Authority, it seems that the functioning of the three EFTA States electronic communication markets in general is not likely to deviate to a larger extent from the average functioning of the markets in the European Union or the whole of the EEA than the functioning of respective markets in individual EU Member States does in comparison with that average.
- (20) The objective of the EEA Agreement is to establish 'a dynamic and homogenous European Economic Area, based on common rules and equal conditions of competition' <sup>(1)</sup>. In light of this objective and the considerations above, the Authority adopts a Recommendation aligned to the Commission's Recommendation in order to ensure uniform application of the common regulatory framework and legal certainty for stakeholders within the electronic communications markets in the EEA. Therefore the number of markets susceptible to *ex ante* regulation is reduced in this Recommendation from 18 to 7 markets.
- (21) The reduction of the number of markets susceptible to *ex ante* regulation does not necessarily indicate that the removed markets are effectively competitive in each of the EFTA States and that *ex ante* regulation is no longer warranted for these markets. Contributions submitted to the Authority during the revision process claim that continued regulation might be justified in certain markets.
- (22) The markets listed in the Annex have been identified on the basis of the three cumulative criteria. For markets not listed in this Recommendation national regulatory authorities should apply the three-criteria test to the market concerned. For the markets in the Annex to Recommendation No 194/04/COL of 14 July 2004, which are not listed in the Annex to this Recommendation, national regulatory authorities should have the power to apply the three-criteria test in order to assess whether, on the basis of national circumstances, a market is still susceptible to *ex ante* regulation. For markets listed in this Recommendation a national regulatory authority may choose not to carry out a market analysis procedure if it determines that the three criteria are not satisfied for the particular market. National regulatory authorities may identify markets that differ from those listed in this Recommendation, provided that they act in accordance with Article 7 of the Framework Directive. Failure to notify a draft measure which affects trade between EFTA States as described in Recital 38 of the Framework Directive may result in infringement proceedings being taken against the State in question. Markets other than those listed in this Recommendation should be defined on the basis of competition principles laid down in the Authority's Notice on the definition of relevant market for the purposes of EEA competition law <sup>(2)</sup> and be consistent with the Authority's Guidelines on market analysis and the assessment of significant market power whilst satisfying the three criteria set out above.
- (23) The fact that this Recommendation identifies those product and service markets in which *ex ante* regulation may be warranted does not mean that regulation is always warranted or that these markets will be subject to the imposition of regulatory obligations set out in the specific Directives. In particular, regulation cannot be imposed or must be withdrawn if there is effective competition on these markets in the absence of regulation, that is to say, if no operator has significant market power within the meaning of Article 14 of the Framework Directive. Regulatory obligations must be appropriate and be based on the nature of the problem identified, proportionate and justified in the light of the objectives laid down in the Framework Directive, in particular maximising benefits for users, ensuring no distortion or restriction of competition, encouraging efficient investment in infrastructure and promoting innovation, and encouraging efficient use and management of radio frequencies and numbering resources.
- (24) The identification of markets in this Recommendation is without prejudice to market definitions in individual cases under competition law. Moreover, the scope of *ex ante* regulation is without prejudice to the scope of activities that may be analysed under competition law.
- (25) This Recommendation has been subject to a public consultation and to consultation with national regulatory authorities and other national authorities in the EFTA States.
- (26) This Recommendation should be interpreted in light of the Explanatory Note of the Commission's Recommendation 2007/879/EC on relevant product and service markets within the electronic communications sector susceptible to *ex ante* regulation in accordance with the Framework Directive. The Explanatory Note includes, inter alia, the description of evolving technologies in relation to the markets defined in the Recommendation,

HAS ADOPTED THIS RECOMMENDATION:

1. In defining relevant markets appropriate to national circumstances in accordance with Article 15(3) of the Act referred

<sup>(1)</sup> 4th consideration in the Preamble to the EEA Agreement.

<sup>(2)</sup> Decision of the EFTA Surveillance Authority No 46/98/COL of 4 March 1998 on the issuing of two notices in the field of competition on the definition of the relevant market for the purpose of competition law within the European Economic Area (EEA), and on agreements of minor importance which do not fall under Article 53(1) of the EEA Agreement (OJ L 200, 16.7.1998, p. 46 and EEA Supplement No 28, 16.7.1998, p. 1).

- to at point 5cl of Annex XI to the EEA Agreement, Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communication networks and services, as adapted to the Agreement by Protocol 1 thereto and by the sectoral adaptations contained in Annex XI to that Agreement, national regulatory authorities should analyse the product and service markets identified in the Annex to this Recommendation.
2. When identifying markets other than those set out in the Annex, national regulatory authorities should ensure that the following three criteria are cumulatively met:
    - (a) the presence of high and non-transitory barriers to entry. These may be of a structural, legal or regulatory nature;
    - (b) a market structure which does not tend towards effective competition within the relevant time horizon. The application of this criterion involves examining the state of competition behind the barriers to entry;
    - (c) the insufficiency of competition law alone to adequately address the market failure(s) concerned.
  3. This Recommendation is without prejudice to market definitions, results of market analyses and regulatory obligations adopted by national regulatory authorities in accordance with Articles 15(3) and 16 of the Act referred to at point 5cl of Annex XI to the EEA Agreement and as adapted to the Agreement by Protocol 1 thereto and by the sectoral adaptations contained in Annex XI to that Agreement (Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communication networks and services), prior to the date of adoption of this Recommendation.
  4. This Recommendation is addressed to the EFTA States.
- Done at Brussels, 5 November 2008.
- For the EFTA Surveillance Authority*
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| Per SANDERUD<br><i>President</i> | Kurt JAEGER<br><i>College Member</i> |
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## ANNEX

**Retail level**

1. Access to the public telephone network at a fixed location for residential and non-residential customers.

**Wholesale level**

2. Call origination on the public telephone network provided at a fixed location.

For the purposes of this Recommendation, call origination is taken to include call conveyance, delineated in such a way as to be consistent, in a national context, with the delineated boundaries for the market for call transit and for call termination on the public telephone network provided at a fixed location.

3. Call termination on individual public telephone networks provided at a fixed location.

For the purposes of this Recommendation, call termination is taken to include call conveyance, delineated in such a way as to be consistent, in a national context, with the delineated boundaries for the market for call origination and the market for call transit on the public telephone network provided at a fixed location.

4. Wholesale (physical) network infrastructure access (including shared or fully unbundled access) at a fixed location.
5. Wholesale broadband access.

This market comprises non-physical or virtual network access including 'bit-stream' access at a fixed location. This market is situated downstream from the physical access covered by market 4 listed above, in that wholesale broadband access can be constructed using this input combined with other elements.

6. Wholesale terminating segments of leased lines, irrespective of the technology used to provide leased or dedicated capacity.
  7. Voice call termination on individual mobile networks.
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