



EUROPEAN COMMISSION

Brussels, 14.6.2010
C(2010)4154

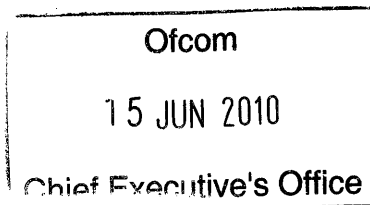
SG-Greffe (2010) D/8320

Office of Communications (Ofcom)

Riverside House
2a Southwark Bridge Road
SE1 9HA
London
United Kingdom

For the attention of:
Mr Ed Richards
Chief Executive Officer

Fax: +44-20 7981 3504



Dear Mr Richards,

Subject: Commission decision concerning case UK/2010/1081: Retail ISDN30 exchange lines services in the UK

Commission decision concerning case UK/2010/1082: Wholesale ISDN30 exchange lines services in the UK

Comments pursuant to Article 7(3) of Directive 2002/21/EC¹

I. PROCEDURE

On 4 May 2010, the Commission registered two notifications from the Office of Communications (Ofcom) concerning the second reviews of the markets for retail and wholesale ISDN30 exchange lines services in the UK².

¹ Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communications networks and services (Framework Directive), OJ L 108, 24.4.2002, p. 33.

² Retail ISDN30 exchange lines, although not listed as such, are part of market 1 listed in the Commission Recommendation 2007/879/EC of 17 December 2007 on relevant product and services 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 communications networks and services (the Recommendation), OJ L 344, 28.12.2007, p. 65. Wholesale ISDN30 exchange lines services, although not listed as such, are similar to services covered by markets 2 and 3 listed in the Recommendation.

The national consultations³ ran parallel with the EU consultations under Article 7 of the Framework Directive. The deadline for the EU consultations is 15 June 2010.

On 18 May 2010, a request for information⁴ was sent to Ofcom. A reply was received on 21 May 2010.

Under Article 7(3) of the Framework Directive, national regulatory authorities (NRAs) and the Commission may make comments on notified draft measures to the NRA concerned.

II. DESCRIPTION OF THE DRAFT MEASURES

II.1. Background

The two notified market analyses build on the reviews of the market for fixed narrowband retail (i.e. analogue and digital (ISDN) telephone lines and calls for residential and business customers)⁵ and wholesale services (i.e. markets covering the supply of wholesale exchange lines, call origination, call termination and various conveyance and transit services that provide connectivity across narrowband networks)⁶, which were put into public consultation in March and September 2009. While the March 2009 consultation still concluded provisionally that BT had significant market power in the relevant retail and wholesale ISDN30 services markets, Ofcom did not arrive at the same conclusion in the September 2009 consultation and held that further assessment was needed, the result of which is presented in the current notifications.

II.2. Market definition

ISDN is a narrowband access service, designed for large business sites, which supports up to 30 channels with a bandwidth of 64 kbit/s per channel and a wide range of services including basic telephony with additional features used exclusively by businesses.

As regards retail markets, Ofcom proposes to continue to define a narrow retail ISDN30 market and excludes new telephony services based on IP-based technology from the relevant market. Ofcom explains that 'hosted VoIP' and IP Centrex services are functionally different from ISDN30⁷. SIP trunking services are closer functional substitutes for ISDN30, but there are relatively few SIP trunks in the UK so far and such services do not offer yet a quality of service and reliability comparable to ISDN30 services. Moreover, customers would need an IP PBX, so they tend to switch largely when there is a need for a wider system upgrade.

Ofcom identifies two distinct geographic markets for ISDN30 retail services: the Hull area and the UK excluding the Hull area.

³ In accordance with Article 6 of the Framework Directive.

⁴ In accordance with Article 5(2) of the Framework Directive.

⁵ See Case UK/2009/0899, the Commission's letter of 3 June 2009, SG-Greffe (2009) D/3172. The residential and business fixed narrowband access and calls services were found to be competitive. Consequently Ofcom now proposes to withdraw the respective financial reporting obligations.

⁶ See case UK/2009/0898, the Commission's letter of 3 June 2009, SG-Greffe (2009) D/3179. Ofcom found that BT retains SMP in the markets for wholesale residential exchange lines for call origination, termination and transit and for ISDN2, and proposed to regulate those markets.

⁷ In addition to exchange line functionality, IP Centrex and Hosted VoIP incorporate the functionality of a PBX and are a substitute for ISD30 only for businesses that are prepared to use a managed network.

As regards the wholesale market, Ofcom includes in the relevant market both ISDN30 exchange lines provided to vertically integrated retailers (self-supply) and exchange lines provided to third-party retailers (e.g. using wholesale line rental, or WLR).⁸ Ofcom explains that other types of access services (e.g. broadband access) cannot be considered to be substitutes given the significant network costs involved (e.g. specific access and backhaul electronics). Hosted VoIP and SIP trunking are not part of the market definition. Ofcom also found that indirect competitive constraints stemming from telephony services based on IP-based technologies are likely to be limited.

Ofcom identifies two distinct geographic markets for ISDN30 wholesale services: the Hull area and the UK excluding the Hull area.

II.3. Finding of significant market power

Ofcom found that no company holds significant market power in the retail ISDN30 access market in the UK excluding Hull. BT's market shares are falling⁹ and barriers to entry are low, especially due to the regulated wholesale access prices; in addition, wholesale line rental allows communications providers (CPs) to offer retail ISDN30 services without any significant investment.¹⁰ Ofcom found KCOM to hold significant market power in the retail ISDN market in the Hull area; its market share is close to 100% and there are no CPs offering ISDN30 via WLR in this area.

Regarding the wholesale narrowband access markets, Ofcom found that Openreach holds significant market power in the supply of wholesale ISDN30 exchange lines in the UK excluding Hull. This assessment is based on the following criteria: (i) market shares¹¹; (ii) barriers to entry and expansion¹²; (iii) prices and profitability¹³, and (iv) countervailing buying power. Ofcom also found that KCOM holds significant market power in the supply of wholesale ISDN30 exchange lines in the Hull area with virtually 100% of the market.

II.4. Regulatory remedies¹⁴

On the retail ISDN30 market, Ofcom proposes to impose two obligations on KCOM: no undue discrimination, and price publication.

On the wholesale ISDN30 market, Ofcom proposes to maintain the remedies currently imposed on Openreach, i.e. obligations: (i) to provide network access on reasonable request (to Openreach's current inputs) and to grant requests for new network access (to

⁸ Self-supply accounts for 79% of all ISDN30 wholesale channels with the remaining 21% of channels supplied by WLR.

⁹ BT's market share (in channels) has fallen from 60% in 2003 to 45% in 2009 (from 69% to 64% in revenue).

¹⁰ In addition to the two large players Virgin Media and Cable & Wireless, BT faces competition from some 300 small WLR providers.

¹¹ Openreach's market share of 67% has remained unchanged since 2003.

¹² The anticipated increase in competition from partial private circuits (PPCs) and other self-supply failed to materialise.

¹³ There had been no change in Openreach's nominal prices, despite a fall in both real and nominal costs, and reported profits were very high (74% of return on capital employed in 2009).

¹⁴ Ofcom clearly differentiates between currently proposed regulatory obligations and BT's undertakings. These are voluntary commitments concerning BT's delivery of products to other communications providers, the internal organisation of BT and which part of BT delivers which product.

Openreach's new inputs), (ii) not to unduly discriminate, (iii) to provide WLR ISDN30, (iv) to publish a reference offer, (v) to notify charges, terms and conditions, (vi) to publish technical information, (vii) to separate its accounts, and (viii) to provide transparency as to the quality of service. Additionally, Ofcom proposes to impose a charge control obligation, given that Openreach is making excessive returns on ISDN30.¹⁵ Furthermore, Ofcom proposes to maintain the current remedies imposed on KCOM, i.e. obligations (i) to provide network access on reasonable request, (ii) not to unduly discriminate, (iii) to publish a reference offer, (iv) to notify charges, terms and conditions, and (v) to publish technical information.

III. COMMENTS

On the basis of the present notifications and the additional information provided by Ofcom, the Commission has the following comments¹⁶:

Impact of IP technology and timeframe of the market review

The Commission notes that Ofcom excludes new telephony services based on IP technology from the ISDN30 retail access market and the ISDN30 wholesale exchange lines markets, given the current impediments to switching (e.g. need of an IP PBX, limited quality of service and reliability) and the fact that the current levels of wholesale and retail prices for ISDN30 are set independently of prices for such IP services. However, Ofcom also explains that ISDN is a product in decline as businesses are increasingly opting for the new IP technologies. In particular, companies carrying out a general system upgrade (e.g. IP-enabled PBX) seem to increasingly consider IP services such as SIP trunking to be substitutes for ISDN30 retail services. This trend and its impact on the wholesale ISDN30 exchange lines market definition and the proposed regulation should be monitored by Ofcom. The timeframe that Ofcom proposes to adopt for the next market review, i.e. four years, is therefore problematic and the Commission stresses that, under Article 16(1) of the Framework Directive, NRAs have to undertake a market analysis at intervals which ensure that ex ante regulation is only imposed and maintained in markets in which, due to a lack of effective competition, ex ante regulation is still warranted¹⁷. Furthermore, the period within which Ofcom undertakes a new market analysis should, in any event, not extend beyond the period provided for under Article 16(6) of the Framework Directive, as amended by Directive 2009/140/EC¹⁸. Against this

¹⁵ Ofcom will consult separately on the detail of the charge control. As an interim remedy between the ending of the market review and the ending of the charge control reviews, Ofcom will impose a safeguard cap applied as a fixed ceiling based on current charges.

¹⁶ In accordance with Article 7(3) of the Framework Directive.

¹⁷ See recital 27 of the Framework Directive, which, for this reason, requires NRAs to carry out market analysis on a forward-looking basis, see also Article 16(1) of the Framework Directive, which requires market analysis to be carried out as soon as possible.

¹⁸ For obligations on the timing of market analyses beyond May 2011 see Article 16(6) of the Framework Directive, as amended by Directive 2009/140/EC, which provides that NRAs must, as a rule, carry out an analysis of the relevant market and notify the corresponding draft measure in accordance with Article 7a within three years from the adoption of a previous measure relating to that market. Directive 2009/140/EC of the European Parliament and of the Council of 25 November 2009 amending Directives 2002/21/EC on a common regulatory framework for electronic communications networks and services, 2002/19/EC on access to, and interconnection of, electronic communications networks and associated facilities, and 2002/20/EC on the authorisation of electronic communications networks

background, the Commission invites Ofcom to closely monitor the market developments of IP-based services on the ISDN30 retail and wholesale markets and carry out a new market review of both markets concerned as soon as relevant new market developments occur.

Pursuant to Article 7(5) of the Framework Directive, Ofcom shall take the utmost account of comments of other NRAs and the Commission and may adopt the resulting draft measures and, where it does so, shall communicate them to the Commission.

The Commission's position on this particular notification is without prejudice to any position it may take *vis-à-vis* other notified draft measures.

Pursuant to Point 15 of Recommendation 2008/850/EC¹⁹ the Commission will publish this document on its website. The Commission does not consider the information contained herein to be confidential. You are invited to inform the Commission²⁰ within three working days following receipt whether you consider that, in accordance with EU and national rules on business confidentiality, this document contains confidential information which you wish to have deleted prior to such publication²¹. You should give reasons for any such request.

Yours sincerely,
For the Commission,
Robert Madelin
Director-General

and services (the 'Better Regulation Directive'), OJL 337, 28.12.2009, p. 37.

¹⁹ Commission Recommendation 2008/850/EC of 15 October 2008 on notifications, time limits and consultations provided for in Article 7 of Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services, OJL 301, 12.11.2008, p. 23.

²⁰ Your request should be sent either by email: INFSO-COMP-ARTICLE7@ec.europa.eu or by fax: +32 2298 87 82.

²¹ The Commission may inform the public of the result of its assessment before the end of this three-day period.