

ETNO RD on ERG draft report on the regulation of access products necessary to deliver business connectivity services



February 2010

Executive Summary

- ETNO welcomes the present consultation and recalls the need for a transparent and balanced approach to interaction with stakeholders by the European Regulators Group (ERG) and the Body of European Regulators for Electronic Communications (BEREC) when developing regulatory guidance for the internal market of the European Union.
- ETNO agrees that national regulatory authorities (NRAs) should assess whether it is appropriate to define a separate market for services supplied to some or all business customers and to analyse the geographic scope of the market carefully, provided this approach is consistently followed at the level of wholesale and retail markets. We believe that a more granular analysis of the markets for services to businesses could create significant scope for deregulation.
- The draft report does not provide evidence of a lack of effective competition on business services markets across EU member states. As such, the report's findings on market definition and remedies are inconclusive. Against this background and notwithstanding the importance of a consistent approach to regulation in the internal market, there appears to be no justification to define a detailed list of "best practice" regulatory remedies in Annex 2 of the report. The Annex should not feature in the final report, unless a far more thorough analysis and justification is provided.

I. General Observations ¹

- On Process –

ETNO welcomes the opportunity to comment on this draft report on business services. As done in our consultative responses to the ERG Work Programme 2009 and Work Programme 2010 (WP 2010), ETNO calls upon the ERG and, in the future, the BEREC to consult on any report with substantive recommendations which potentially influence the decisions by its member NRAs -- and thus have potential material effect on industry stakeholders. We are pleased to see that the ERG has responded to this call in this consultation and hope this will be the case in the future.

ETNO, though, would like to express its concern about the process leading to the present draft report:

- Prior input to ERG by selected stakeholders, which is repeatedly referenced in the draft report, has not been made publicly available;
- Only summaries of the survey results conducted by the ERG are reported. ETNO thinks it would be appropriate – and good practice – for the ‘raw’ responses to the three questionnaires referred to in the “Evidence” section to be made public. Of particular interest would be a more detailed account of the responses to “Questionnaire 3 on retail market experience” from INTUG member companies, such as the identity of the “medium-sized member state” from which the bulk of the responses came. This is especially relevant as ERG itself has questions about the representative character of some of the survey results;
- The consultation period, effectively four weeks given the year-end holiday break, is very short. In addition, insufficient time was foreseen between the date of the ERG public workshop on the consultation, i.e., 29 January 2010, and the deadline for submission of the replies, i.e., 1 February 2010. This makes it practically impossible to include, in the submission to the consultation, any sort of reflexions that may come out of the public workshop. This appears very much to be a missed opportunity and to reduce the quality of the consultation overall.

There is thus much potential for improving the process of developing regulatory guidance by the ERG and BEREC in the future as concerns transparent interaction with stakeholders.

¹ TDC does not support this Reflection Document.

- On the lack of relevant evidence -

The investigation of ERG shows no conclusive finding of a lack of effective competition in the investigated market segments on the basis of present regulation. The ERG reports that the majority of NRAs did not have to deal with any complaints regarding the provision of business services in the past market review (p. 7). Also the concentration of responses to the INTUG questionnaire in one member state indicates that the investigated segments display no significant competition problems across the internal market. Furthermore, ERG concludes that judging from disputes in the market *“there does not seem to be a pressing or strong demand by users or operators”* for segmenting different markets in the area under investigation. The investigation, says the draft report, *“has not proved or disproved that there is a lack of effective competition.”* Numerous other statements within the report, not produced here, reveal the inconclusive nature of the investigation.

In line with these findings, we would expect the ERG to refrain from making specific Recommendations to its member which go beyond high-level suggestions, such as the *“preliminary findings”* on p. 21. The draft report, though, contains a detailed list of so-called *“best practice”* regulatory remedies in Annex 2 of the draft – regulatory remedies which will inform the revision of ERG(07)54 *“Common Position on Best Practice in Remedies Imposed as a Consequence of a Position of Significant Market Power in the Relevant Markets for Wholesale Leased Lines”* foreseen in WP 2010. The current analysis, however, does not support these recommendations. ETNO is concerned with this apparent incoherence: on the one hand, the inconclusive finding of the investigation and on the other hand the concrete guidance on the imposition of business services-specific remedies. ETNO therefore maintains that Annex 2, in absence of a far more thorough empirical analysis and justification, should no longer be included in the final report (s. below, III.).

II. Market definition issues

In the *“Preliminary findings”* section at the end of the proper report, the ERG makes two broad findings with regards to market definition:

- It is appropriate for regulators to assess whether it is necessary to define a separate wholesale market for services supplied to some or all business customers;
- The geographic scope of the wholesale market (for services offered to multi site business users) could differ (from that of the market for services offered to consumer and single site business customers).

ETNO in principle welcomes these preliminary findings, assuming that they are applied consistently at wholesale and retail level (s. below). ETNO believes that a more granular analysis of the markets for services to businesses would create significant scope for deregulation.

The regulation of access products must follow from the analysis of one or more relevant markets. The more detailed the analysis of each market by customer and service the more likely it is to identify real differences between distinct markets where competition is effective or not. Where findings of significant market power (SMP) are limited to those specific markets where competition is not effective and there is no tendency towards effective competition, the remedies to address that specific market failure will lead to more proportionate regulation. ETNO invites the ERG to include in its final report the following observations in this regard:

- Market definition in the context of market analyses under the Regulatory Framework for electronic communication must commence at the retail level.ⁱ A differentiation between residential, small business and high-end business customers at the wholesale level will likely be mirrored in the retail market definition as regulation on a related wholesale market can only be justified if there is a specific market failure on a corresponding retail market that needs to be tackled. Generally, if there is a dedicated demand for wholesale products for high-end business customers, NRAs would also identify a distinct retail market. This should be more clearly recognised in the discussion of market analysis issues in the final report;
- Contrary to the observations referred to by the ERG and as per reports on low margins, retail markets for services to high-end business customers in Europe tend to be highly competitive. Pan-European and global competitors for ICT business and connectivity solutions fiercely compete among themselves and with former incumbents on their home markets.ⁱⁱ A definition of distinct retail markets for high-end business customers would likely lead to a deregulation of this market segment.
- Wholesale access services delivered to the market for services offered to consumer and small single-site business customers (bitstream, partial private circuits (PPCs) up to 2 Mb/s, low speed Ethernet access) almost invariably use the incumbent operator's ubiquitous copper network. In contrast, access services to high-end business customers at higher speeds utilise optical fibre access and point-to-point radio to deliver higher speed economically. The costs faced by the incumbent operator to build or extend a fibre or radio access network may be the same or greater than those faced by entrants using competing networks.ⁱⁱⁱ Both market analyses and remedies for market failure should recognise the differences in the economics for high bandwidth and low bandwidth wholesale access services. Own investment by an

alternative operator in network capacity required to provide services to high-end business customers may therefore be economically more viable than a duplication of existing low bandwidth wholesale service based on copper or low capacity leased lines for residential or small business customers would be. The draft report (on p. 19) rightly points out the more complex nature of contracts and the higher willingness to pay of large business customers. Markets for serving “high-end” business customers are therefore likely to be characterised by lower barriers to entry, and tend towards effective competition respectively, as entry barriers can be overcome. When assessing competition in the market, in addition to the presence and competitive position of alternative operators, NRAs should also take into account that business connectivity services are often already provided by the incumbent to other operators on a wholesale commercial basis.

- Wholesale markets for serving high-end business customers are therefore more likely to not fulfil the “three criteria test” for the application of sector-specific regulation. ETNO encourages the ERG to reiterate in its report that NRAs should conduct the three criteria test on any market – especially if defined differently from those listed in the Annex to the Recommendation on relevant markets - before regulatory obligations based on a SMP-finding can be imposed;
- The wholesale markets for services offered to multi-site businesses show great geographic variation within member states for a number of reasons. Within metropolitan areas the greater density of demand high end business services leads to additional network build. In these locations the SMP operator’s network may be competing with cable TV networks, new entrant fibre built to business parks, wireless network providers targeting business services, or even state investment in fibre networks that are available to all downstream competitors on an open access basis. The presence of competing infrastructures should inform each step of the regulatory process - the market analysis, the geographic sub division of the market for SMP designation, and the nature of the remedies imposed on an SMP operator.

Notwithstanding these observations, ETNO believes that defining a general rule for the delineation of separate business customer markets or geographically differentiated markets would not be appropriate, as any such finding is case-sensitive and therefore has to be determined within the individual market analysis in accordance with the framework.

III. Issues related to the imposition on remedies

In the “Preliminary findings” section at the end of the proper report, the ERG finds that even where a single market is defined, regulators should consider whether there should be a separation of remedies to differentiate between (regulated wholesale access products to serve) high end business users and (to serve) standard users. Such a differentiation of remedies within one market could be a useful instrument to target regulation to the specific market failure identified. In this respect, we refer to the ERG common position on geographic aspects of market analysis of October 2008, in as far as it concerns geographic differentiation of remedies finding that *“within a national market it could still be the case that there exist geographic differences in competitive conditions which do not vary so much that it undermines the finding of a national market but which may lead to differences in identified competition problems and hence differences in appropriate remedies. In such cases any geographic differentiation of remedies needs to be based on a thorough analysis of the market power including potential competition”*.

In the absence of separate markets for wholesale access services for business users and residential users, the need for specific obligations in this field will have to be argued in detail and justified on the basis of an identified market failure at retail level.

However, there appears to be no justification for defining the detailed obligations listed in current Annex 2 of the draft as “best practice” remedies for ERG/BEREC monitoring. This discrepancy is our main concern with the draft.

ETNO has consistently cautioned against a mere ‘tick-list’ approach to remedies applied by ERG in past “best practice” documents for wholesale markets. The imposition of regulatory remedies in such markets should be carefully targeted to the market failure identified in the relevant market aligned with the requirement of proportionality under the Regulatory Framework. ETNO acknowledges that in the business segment with international multi-site customers, consistency of regulatory approaches to access regulation throughout Europe can be beneficial. However, in the absence of empirical findings on a pan-European basis, the mere claim that all the “various obligations” listed in the draft Annex II have the potential to improve competition in the markets concerned alone clearly could not justify their recommendation as best practice.

We also note that some of the obligations listed, such as the general non-discrimination obligation, while undoubtedly contributing to a competitive retail market in the presence of SMP are not specific to business services market(s) (segments).

Additional ETNO comments concern:

1. SLAs (pts. 2 – 10 of Annex II)

Many detailed elements of regulatory obligations are successfully and efficiently covered in contractual agreements of market parties. Regulatory prescriptions on a detailed level should always be an exception.

Service level agreements (SLAs) are a requirement for high-end business customers when they tender for data networks so as to allow them to assure the continuity of business critical data and information technology (IT) applications. In the absence of network performance data, any SLA is basically a ‘insurance policy’ where a (price) premium is paid by the customer in the expectation of recovering some -- or all -- of that premium when the network performance fails to deliver contracted levels and the service providers incurs penalties. If network providers to publish network performance data then sales staffs, high-end business, and wholesale customers can all know what service levels are achievable.

Network operators resisting attempts to set reasonable key performance indicators (KPIs) and publish their performance against these KPIs run the risk of losing the trust of key customers as to the levels of service that their networks can actually deliver.

As the paper states, companies are willing to pay higher prices for dedicated SLAs for business customers. If there is demand for such dedicated SLAs, network operators will generally offer such services to benefit from these higher payments. This is a typical market-driven mechanism.

2. First mover advantage regarding new retail products (pt. 13 of Annex II)

Contrary to the position stated in pt. 13, ETNO believes that access regulation in market 5 and 6, where applicable, should not automatically extend to wholesale inputs for new retail offers, unless the need for such access products has been determined by a market analysis (s. ETNO RD 307 2009 on the draft Commission NGA Recommendation, p. 16).

ETNO fully acknowledges the role of a non-discrimination obligation to ensure effective competition downstream, whenever wholesale inputs are required to compete with a market dominant undertaking. But any new access obligation needs to be proportionate and justified in the light of actual market conditions. For example, wholesale inputs to “new” retail products may be available on a commercial basis on

appropriate terms and conditions, which would be preferable to prescriptive regulatory solutions. Equally, an access obligation would be disproportionate if competitors have the ability to install competing facilities or make use of basic access products to build the service themselves (cf. Art. 8 (2) Access Directive). In any event, the regulation of new products can only arise following detailed competition assessment in the context of a market analysis.

ETNO recalls that the introduction of new retail products by the market dominant undertaking is also part of the competitive process, driving innovation in the market. Across-the board obligations as the one proposed in pt. 13 could in this respect hold back innovation and competition.

3. Proposed access obligations to provide services not supplied to internal downstream businesses (pts. 14, 15 of Annex II)

ETNO is concerned about the following proposed plan for future work:

“ERG plans to consider further the question of whether – and if so, under what circumstances - NRAs should be entitled to impose on SMP players proportionate and objectively justifiable obligations to supply services which they do not at present supply to themselves” [emphasis added].

As with several NRAs referred to in the draft report, ETNO maintains that SMP players cannot be required to deliver services other than those which are the same as – or substantially equivalent to – the services which they supply to themselves.

We concur with the ERG that the question “is a general one which goes well beyond the scope of regulation of business services.” If the ERG is indeed considering this issue generally, ETNO calls upon the ERG to treat it in a transparent manner, e.g., via a public consultation. In the interim, we offer some preliminary views.

The Regulatory Framework contains clear criteria which must be satisfied before new obligations can be imposed on an SMP operator. In summary, these are that the obligation must be imposed as an appropriate remedy to competition issues identified in accordance with the principles set out in the Access and Framework Directives, and the obligation must be necessary, proportionate and justified relative to the problem it is intended to address. The need to

encourage investment in infrastructure is a key consideration in this analysis, as is the ability to install competing facilities (Art. 8, 12 (2) Access Directive).

Any potentially new obligations on an SMP operator to provide access must be imposed as appropriate remedies to competition problems identified on retail markets in accordance with the principles of competition law and in accordance with the principles set out in the Access and Framework Directives. As non-discriminatory access to key wholesale inputs under appropriate conditions would normally ensure effective competition at the retail level, it is difficult to imagine how the imposition of access variants not offered by the regulated operator to its own retail operations could be justified under the present framework.

In this regards, the ERG has stressed^{iv}: “the importance of the role of economic analysis in being capable to identify the types of competition problems and the remedies to these problems in an effective and self-sustaining manner. Of particular importance in this regard is the question of the proportionality of the remedy”[emphasis added].

4. Observations on the Development of Business Connectivity Markets

To conclude, we would like to share some general observations on the development in the markets relevant to business connectivity that ETNO members experience.

Retail business connectivity services cover a multitude of different services. Traditionally, these would have been supplied using leased lines and classical switched data services, such as Frame Relay and asynchronous transfer mode (ATM). Leased Lines provided point to point dedicated capacity for data transfer between business customers. Frame Relay and ATM allowed switching of data streams between multiple sites but essentially used leased line access into each individual site. The high cost of providing and managing dedicated capacity delivered across time division multiplexed (TDM) networks - and the resulting leased line pricing – meant that transfer speeds were limited and the services were only suitable for very high value business critical (and largely real time) applications.

With the introduction of Internet Protocol (IP), business connectivity services have changed as high-end business customers discovered a requirement for high capacity connectivity to the public Internet as well as running business applications that were more ‘bandwidth-hungry’ but (generally) less time critical. This encouraged

communications providers to design connectivity solutions with new features, using packet switching techniques in the core.

All European incumbents and many entrants are building next generation networks (NGNs), and these networks have many common features across national boundaries. Each network will have a core where service demands are switched between nodes as packets. These core networks are supplemented with access networks to deliver business connectivity services from the edge of the core to the customer premises.

These changes in the way business services are provided may have an impact on market definitions / the attribution of products to certain markets and on the nature of remedies which may be imposed to ensure effective competition on retail markets for “high-end” business services. If such changes in market definition or remedies occur, NRAs have to ensure consistency with - and if relevant make the necessary adaptations to - the currently existing regulation for markets 5 and 6.

i Explanatory Memorandum to the Commission Recommendation on relevant product and services markets SEC(2007) 1483/2, p. 13

ii Pan-European operators active in the provision of VPN solutions in the EU are, for example. BT Global Services, Orange Business Services, AT&T, Verizon, T-Systems, COLT, Reliance Globalcom, Easynet Global Services

iii We note that in the future, this situation may justify an analysis of a more symmetrical approach to regulation for this market segment, comparable to the situation where an investor in residential fibre who is not the incumbent may be required to grant access on a symmetrical basis under the revised EU Regulatory Framework.

iv ERG (06) 33, “Revised ERG Common Position on the approach to Appropriate remedies in the ECNS regulatory framework,” May 2006.