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Onafhankelijke Post en
Telecommunicatie Autoriteit
(OPTA)

Zurichtoren - Muzenstraat 41
2511 WB Den Haag
Netherlands

For the attention of:
Mr. Chris A. Fonteijn
Chairman

Fax: +31 70 315 92 04

Dear Mr Fonteijn,

**Subject: Commission decision concerning Case NL/2012/1306: Fixed
Telephony Markets in the Netherlands**

Article 7(3) of Directive 2002/21/EC¹: No comments

I. PROCEDURE

On 16 March 2012, the Commission registered a notification from the Dutch national regulatory authority, the Onafhankelijke Post en Telecommunicatie Autoriteit (OPTA), concerning the fixed telephony markets in the Netherlands (wholesale and retail)².

The national consultation³ ran from 14 July 2011 for a period of 8 weeks. Interested

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, as amended by Directive 2009/140/EC, OJ L 337, 18.12.2009, p. 37, and Regulation (EC) No 544/2009, OJ L 167, 29.6.2009, p. 12.

² Corresponding to markets 1 and 2 in Commission Recommendation 2007/879/EC of 17 December 2007 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 communications networks and services (Recommendation on Relevant Markets), OJ L 344, 28.12.2007, p. 65, and markets 3 and 5 in Commission Recommendation 2003/311/EC of 11 February 2003 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 communications networks and services, OJ L 114, 8.5.2003, p. 45.

parties were also invited to a public hearing on 2 September 2011.

On 28 March 2012 a request for information⁴ was sent to OPA and a response was received on 2 April 2012.

Pursuant to Article 7(3) of the Framework Directive, national regulatory authorities (NRAs), the Body of European Regulators for Electronic Communications (BEREC) and the Commission may make comments on notified draft measures to the NRA concerned.

II. DESCRIPTION OF THE DRAFT MEASURE

II.1. Background

The market for fixed telephony in the Netherlands was previously notified to and assessed by the Commission under cases NL/2008/0821, NL/2008/0822 and NL/2012/1303.

II.2. Market definition

To identify the appropriate wholesale market delineation, OPA starts by analysing the retail market in the absence of regulation. OPA identifies, on the basis of supply-side substitution and potential competition as well as demand-side substitution, three national retail markets which are reflected at wholesale level:

- (i) PSTN/VoB1 access and calls (single calls market),
- (ii) ISDN1/ISDN2/VoB2 access and calls (dual calls market), and
- (iii) ISDN15/ISDN20/ISDN30 access and calls (multiple calls market).⁵

Similar to its 2008 regulatory decision for fixed telephony, OPA finds access and calls to be part of the same product market since in the Netherlands 98% of customers take the access subscription and call services from one and the same provider.⁶ OPA finds that all access/call services delivered over copper, fibre and coaxial cable networks belong to the same relevant wholesale markets which are national in scope. OPA considers that in the presence of wholesale regulation the scope of the identified retail markets is not altered.

³ In accordance with Article 6 of the Framework Directive.

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

⁵ OPA refined the market definition, compared to its previous decisions from 2005 and 2008, which made a distinction between a "residential" market (two or less simultaneous connections) and "business" market (more than two simultaneous connections). OPA now considers it appropriate to make a distinction between single and dual calls in order to accurately reflect the competitive pressure exerted by VoB services: OPA observed relatively significant pressure of VoB on the single calls market, while it found only a limited impact on the dual calls market. Maintaining the joint market for single and dual calls would not reflect the pressures exercised by VoB. Further, the two markets have some differences in their demand characteristics, which are reflected in their pricing.

⁶ OPA explains that in a greenfield approach, there would be no stimulus to provide access to the fixed telephony network separately from the calls services. In the presence of wholesale regulation, including C(P)S regulation, by Q2 2011 only 2% of end-users still take the two services from separate providers.

II.3. Assessment of the three-criteria test⁷

OPTA concludes that the three-criteria test is met with regard to the wholesale markets for single, dual and multiple calls.

OPTA considers that, in the presence of wholesale regulation (i.e. carrier (pre-)selection (C(P)S) and wholesale line rental (WLR)) as well as significant pressure from voice over broadband (VoB) services, the retail market for single calls⁸ tends to effective competition, hence the second criterion of the three-criteria test is not met.

OPTA concludes that the retail dual and multiple calls markets instead do meet the three-criteria test, making them susceptible to ex ante regulation.

II.4. Finding of significant market power

II.4.1. Wholesale markets

OPTA finds KPN to have SMP on all three relevant wholesale markets on the basis of the following: market shares; infrastructure that is difficult to duplicate; vertical integration; products and services diversification; economies of scale and scope (which remain important, despite the presence of upstream generic wholesale regulation, in combination with network coverage); barriers to switching; absence of countervailing buyer power; and barriers to entry (albeit lessened in the presence of upstream wholesale generic access regulation).

With regard to market shares, OPTA finds KPN to have, in the presence of upstream generic wholesale regulation, a share of [...] % on the single calls market in Q2 2011. This share is expected to grow (to an estimated 57%) by the end of 2014, despite the expected strengthening of the position of cable operators, due to the foreseen growth of VoB services⁹, as well as of alternative operators providing services on the basis of generic wholesale regulation.

On the dual calls market, OPTA finds that KPN's Q2 2011 market share of [...] % is likely to still be as high as 87% in the presence of generic wholesale regulation at the end of 2014. Cable operators recently entered the market with their VoB services but have not yet established a strong market position.¹⁰

On the multiple calls market, OPTA finds that KPN's Q2 2011 market share of [...] % is

⁷ In accordance with Point 2 in conjunction with Recital 5 of the Recommendation on Relevant Markets, when identifying markets other than those mentioned in the Annex, national regulatory authorities should ensure that the following three criteria are cumulatively met: (1) there must be high and non-transitory entry barriers, (2) the structure of the market must not tend towards effective competition within the relevant time horizon and (3) the application of competition law alone would not adequately address the market failure(s) concerned.

⁸ In its 2008 analysis of the retail fixed telephony market in the Netherlands, OPTA found KPN not to have SMP on the residential segment which included two or less (simultaneous) calls by means of PSTN, VoB1 and ISDN2 and VoB2. OPTA explains that the corresponding currently identified single calls market which includes only (stacked) PSTN and VoB1 call services is even more competitive than the 2008 residential market. KPN's market share which was [...] % in mid-2010 and [...] % in mid-2011 is expected on the basis of four potential scenarios to lie between 46 and 56% at the end of 2014.

⁹ OPTA notes however that some PSTN customers do not yet switch to VoB due to specific needs for alarm systems and/or not requiring a bundle of services (with TV and/or internet). OPTA considers that VoB is a better substitute for ISDN than for PSTN connections.

¹⁰ Of the total number of connections on the dual calls market, [...] % relates to VoB. VoB services are becoming increasingly important on this market. Of KPN's market share, [...] % relates to VoB-based dual call services.

likely to still be as high as 67% at the end of 2014. On this market the role of cable operators is limited, due to the limited network coverage of the individual operators and the fact that VoB-services are not included in this market.¹¹

II.4.2. Retail markets

OPTA finds KPN to have SMP on the dual and multiple calls markets inter alia on the basis of market shares, infrastructure that is difficult to duplicate, network coverage, economies of scale and scope, and barriers to switching.

On the dual calls retail market, OPTA finds that KPN's [...] % market share in Q2 2011 is expected to decrease to 70-85% in the presence of wholesale regulation. In this regard, OPTA indicates that, according to market studies, the importance of WLR for the delivery of ISDN2 will decrease, at least in the long term, due to the increase in importance of VoB. On the bottom part of the SOHO¹² market there is an increase in bundles with VoB. The growth potential of cable operators is considered however less strong than on the single calls retail market as they have not yet rolled out their coax networks to business areas and they mainly offer exclusively VoB, while the business market retains an interest in ISDN.

Furthermore, KPN has a nation-wide copper access network, differently from the individual cable operators. Wholesale access, C(P)S and WLR regulation diminish KPN's competitive advantages in terms of (i) network coverage, (ii) infrastructure that is difficult to replicate and (iii) advantages of vertical integration. KPN, however, benefits from economies of scale and scope, and to a limited extent from advantages of product and services diversification, even in the presence of wholesale regulation, particularly because of its mobile telephony capacity. Barriers to switching and disciplining effects from outside the market also play a role in KPN's SMP position on this market.

On the multiple calls retail market, OPTA finds that KPN's [...] % market share in Q2 2011 is likely to decrease to 56-66% by the end of 2014. However, several factors contribute to the finding of KPN's SMP position on the market: limited dynamics on the retail market for multiple calls services; KPN's difficult to duplicate network coverage and vertical integration; economies of scope and to a limited extent economies of scale; product and services diversification; switching barriers; and lesser disciplining effect of potential transfers of call volumes.

II.5. Regulatory remedies

II.5.1. Wholesale regulation

OPTA finds that KPN has the possibility to engage in anti-competitive behaviour such as refusal of access, discriminatory behaviour (in terms of information provision, delaying tactics, access conditions, quality, strategic product design, tying, pricing), margin squeeze and excessive pricing. To remedy such potential market failures ex ante, OPTA proposes to impose on KPN the following obligations:

- (i) C(P)S, including further call origination services (destinations by means of which follow-up services can be provided) and associated facilities for the delivery of PSTN and ISDN connections and single, dual and multiple call services;¹³

¹¹ OPTA explains that while VoB is a retail demand substitute for ISDN1/2, it is not yet to a sufficiently extent for ISDN15/20/30 due to the perception of lower quality (related to latency and jitter) in combination with relatively high switching barriers in terms of costs.

¹² Small Office / Home Office

¹³ In its draft measure, OPTA lists the numbers that are concerned by this obligation.

- (ii) *WLR*, including associated facilities, allowing the access seeker to take over the customer relationship, which can be seen as a supporting measure to C(P)S for the delivery of PSTN and ISDN connections and single, dual and multiple call services.

In support of these obligations, OPTA proposes to impose:

- (ii) *non-discrimination*, including a tariff differentiation¹⁴ and a margin squeeze¹⁵ prohibition;
- (iii) *transparency*, including the publication of a reference offer;
- (iv) *tariff regulation*, based on a safety cap with an inflation corrector and a wholesale price cap based on embedded direct costs (EDC)¹⁶ for new services for dual and multiple calls services. OPTA acknowledges that this does not correspond to strict cost orientation but explains that in the light of uncertain market developments for at least the next 10 years, the market needs regulatory certainty¹⁷. Against this background, OPTA proposes already now to maintain this regulation for several regulatory periods.

OPTA will ease regulatory intervention by way of withdrawing the obligation of C(P)S or WLR for the provision of VoB. Such regulatory easing is proposed to become effective upon entry into force of the revised telecom package in Dutch law, after which OPTA must specify which specific forms of access are concerned by the access obligation¹⁸.

OPTA does not find it necessary to maintain C(P)S regulation with regard to VoB connections as generic wholesale obligations such as local loop unbundling on the physical network infrastructure market and wholesale broadband access (WBA) are better suited¹⁹. OPTA also does not find it necessary to maintain the WLR obligation with regard to the provision of VoB as it would restrict the investment incentives of VoB providers and can very well be delivered on the basis of WBA. In fact, at that point, OPTA does not propose any regulation with regard to VoB services at the wholesale level.

¹⁴ Some forms of tariff differentiation may however be applied after approval by OPTA

¹⁵ This prohibition is specified in non-discrimination rule number 5 which stipulates that KPN's downstream services must be at all times and all cases be replicable, at services level, in terms of pricing. The retail increment is set at 1%, reflecting retail costs that are purely incremental to a particular single service.

¹⁶ In the EDC system, all costs which are relevant for the supply of a given wholesale service, i.e. indirect, joint and common costs, are allocated to that service. Current cost accounting (CCA) is applied.

¹⁷ The Commission notes that OPTA proposed tariff regulation based on a safety cap also for market 4 (case NL/2011/1278), which has led the Commission to make a comment on the appropriateness of cost oriented access prices for wholesale access products. The Commission notes the greater flexibility (within the boundaries of the Regulatory Framework) that NRAs are afforded in setting remedies, where there is no adopted recommended approach pursuant to Article 19 of the Framework Directive. In this specific case, the Commission considers it not appropriate to repeat the comment made in case NL/2011/1278, which was made taking into account the Commission's recommended approach for setting cost oriented prices for next generation access products.

¹⁸ The Commission has in this respect repeatedly expressed its concerns as regards the late transposition of the revised regulatory framework in the Netherlands.

¹⁹ OPTA specifies that in case a provider asks KPN for C(P)S access for the delivery of VoB, parties will first have to seek a commercial agreement and OPTA will verify whether it concerns a reasonable request and whether an exception should be made to the rule.

Further, for single calls services OPTA does not consider it proportionate to continue tariff regulation after transposition and entry into force of the revised telecom rules. According to the current Dutch Telecommunications Act OPTA must impose C(P)S price regulation on parties designated with SMP. Under the revised Dutch telecom law this clause will be repealed. OPTA considers that the non-discrimination obligation removes the incentive for KPN to charge excessive prices. The migration from PSTN to VoB and the strong position of cable operators on VoB will motivate KPN to set tariffs that will allow its customers to compete with cable operators.

OPTA considers that on the dual and multiple calls market, the risk of customers switching to cable or other providers with their own infrastructure is limited and that therefore price regulation remains necessary.

II.5.2. Retail regulation

In the presence of wholesale regulation and following the analysis of the three criteria test, OPTA finds that KPN still has SMP and the possibility and incentive to engage in anti-competitive behaviour on the dual and multiple call services markets with regard to ISDN connections, e.g. excessive pricing, margin squeeze, price discrimination and tying or bundling. To remedy such potential market failures ex ante, OPTA proposes to impose a price floor obligation, under the form of a price squeeze test at services level whereby the increment will be set on the level of the integral retail costs that need to be covered by KPN, based on KPN's (to be published) 2011 costing data.

OPTA considers that in the light of the very limited group of inert customers that could be subject to excessive pricing by KPN, it is not proportionate to impose other specific regulation. OPTA explains that the price floor obligation will promote services competition and competitive pressure on KPN not to charge excessive prices. Similarly, the price floor obligation ensures the price-replicability of KPN's offers and thus hampers anti-competitive bundling practices. Competition law could tackle lock-in practices should they occur.

With regard to dual calls VoB services (note that VoB services are not included in the market for multiple calls), OPTA does not propose to maintain the previously imposed price regulation (price floor). OPTA considers that this is not necessary in view of the lack of advantages for the KPN, the existence of wholesale offers provided by KPN that can be used to provide VoB services, and the margin squeeze test. OPTA also considers that cable operators have started to enter into the dual calls market, and they will increase their market share in the future.

The retail obligation as imposed in OPTA's 2008 retail fixed telephony market analysis will be withdrawn and replaced in line with the implementation periods of the currently proposed remedies.²⁰

III. NO COMMENTS

The Commission has examined the notification and the additional information provided by OPTA and has no comments.²¹

Pursuant to Article 7(7) of the Framework Directive, OPTA may adopt the draft measure

²⁰ Price modifications required with regard to the active portfolio shall be carried out within three months following the entry into force of the presently notified measure. The implementation period for the installed base amounts to nine months after entry into force of the presently notified measure.

²¹ In accordance with Article 7(3) of the Framework Directive.

and, where it does so, shall communicate it 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/EC²² 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 Commission²³ 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 publication.²⁴ You should give reasons for any such request.

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

²² 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, OJ L 301, 12.11.2008, p. 23.

²³ Your request should be sent either by email: INFSO-COMP-ARTICLE7@ec.europa.eu or by fax: +32 2 298 87 82.

²⁴ The Commission may inform the public of the result of its assessment before the end of this three-day period.