



EUROPEAN COMMISSION

Brussels, 1/06/2010
C(2010)3615

SG-Greffe (2010) D/7658

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/2010/1064: Wholesale local access market

Commission decision concerning case UK/2010/1065: Wholesale broadband access market

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

I. PROCEDURE

On 23 March 2010, the Commission registered two notifications from the Office of Communications (Ofcom), one concerning the second review of the market for wholesale local access (WLA) services² the other the third review of the market for wholesale broadband access³ (WBA) in the UK.

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 This market corresponds to market 4 in 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.

³ This market corresponds to market 5 in the Recommendation.

The national consultations⁴ run in parallel with the EU consultations under Article 7 of the Framework Directive. The deadline for the EU consultations is 1 June 2010.

On 20 April 2010, a request for information⁵ was sent to Ofcom. A response was received on 23 April 2010.

Pursuant to 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

II.1.1. The wholesale local access market

Under case number UK/2004/0094, Ofcom notified the Commission of its review of the market for wholesale unbundled access (including shared access) to metallic loops and sub-loops for the purpose of providing broadband and voice services in the United Kingdom, comprising both traditional copper local loops and cable connections. Ofcom concluded that BT should be designated as the operator having significant market power (SMP) in the UK excluding the Hull area, where Kingston Communications (KCOM) was designated as the operator with SMP. Consequently, Ofcom proposed to impose regulatory obligations on both operators. In the letter containing its comments the Commission raised issues concerning the inclusion of both copper loop-based and cable-based wholesale local access in the definition of the product market.

II.1.2. The wholesale broadband access market

The first review of the market for wholesale broadband access was notified to and assessed by the Commission earlier under case number UK/2003/0032-0034. At the time, Oftel segmented the wholesale broadband access market into the UK area (excluding Hull) and the Hull area⁶. Oftel designated BT as the operator holding SMP in the UK (excluding Hull) and KCOM as the SMP operator in the Hull area and, consequently, imposed regulatory obligations. The Commission commented on the inclusion of cable-based services in the market definition, based on the indirect pricing constraint exerted on DSL-based services at retail level. However, the Commission concluded that exclusion of cable would not have altered the conclusions drawn by Oftel.

In its second round of analysis of the wholesale broadband access market (case UK/2008/0733), Ofcom proposed to segment the market regionally and defined the following relevant geographic markets: (i) the Hull area: where only KCOM is present; (ii) market 1: local exchanges where only BT is present; (iii) market 2: local exchanges with two or three principal operators⁷ and exchanges where four or more principal

⁴ In accordance with Article 6 of the Framework Directive.

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

⁶ Asymmetric broadband origination and conveyance in the UK (excluding Hull) and asymmetric broadband origination in Hull.

⁷ Operators which provide broadband services over their own access networks (BT or Virgin Media) or which have deployed LLU in more than 10% of the UK. Virgin Media was considered to be a principal operator in an individual exchange area only if it was able to provide services to 65% or more of the delivery points.

operators are forecast, but where the exchange serves fewer than 10000 premises; (iv) market 3: local exchanges with four or more principal operators and exchanges where four or more principal operators are forecast, but where the exchange serves more than 10000 premises. Ofcom concluded that there was no SMP operator on market 3. As regards the other regional markets, BT was considered to have SMP on markets 1 and 2 and KCOM was found to have SMP in the Hull area. Ofcom proposed to impose regulatory obligations on the markets where BT or KCOM were found to be the SMP operators.

In the letter containing its comments the Commission stated, *inter alia*, that definition of geographic sub-markets had to be based on a thorough analysis of structural and behavioural factors. This should include not only structural indicators, such as the number of competitors present in a given exchange area, but also other potentially relevant factors, such as the size/density of the areas in question, in order to establish that the presence of alternative operators is sustainable. The distribution of market shares and their development over time within individual exchange areas should also be looked into. Relevant behavioural indicators would include a preliminary analysis of pricing, price trends and price differentiation at retail and wholesale level and also any differences in supply and demand patterns, such as the commercial strategies observed and products/services offered in the different areas. Definition of geographic sub-markets would also entail assessing whether any proposed market boundaries would be sufficiently stable over time.

II.2. Market definition

II.2.1. Wholesale local access

Ofcom proposes to define the relevant WLA market as including copper-based, cable-based⁸ and fibre-based⁹ local access at a fixed location. It excludes mobile-based, fixed wireless-based and satellite-based WLA. In addition, Ofcom proposes to include self-supply in the market definition and to have a single WLA market for lines for business and residential use.

In order to define the boundaries of the WLA market, Ofcom assesses the changes in the network occurring or expected to occur over the next few years due to the deployment of next-generation access (NGA) networks. Ofcom concludes that, although in the past WLA and WBA products were differentiated on the basis of their physical and non-physical nature, the newly deployed FTTC and FTTH network architectures mean that non-physical products that have underlying characteristics consistent with physical products should be included in the same market. Accordingly, Ofcom defines certain key characteristics (i.e. localness¹⁰, minimum functions incorporated¹¹, service-agnostic¹² and

⁸ Ofcom proposes to include cable-based services within the relevant market on the basis of indirect constraints, relying on the evidence available from previous reviews.

⁹ BT and Virgin Media both now offer retail services that are based on NGA networks. According to Ofcom, BT's current plan for deploying its NGA network runs to the end of 2012, by which time it aims to cover around 40% of UK premises. Under BT's plans, three quarters of those premises would be supplied by fibre-to-the-cabinet (FTTC) and the rest by fibre-to-the-premises (FTTP) technology.

¹⁰ The product should be available at a location close to the end-customer, as LLU is.

¹¹ The inherent capability of the access technology is made available and the service is undimensioned, which allows communications providers (CPs) to change and control the functions and quality of services.

dedicated capacity¹³) of WLA products independently of their physical or non-physical nature.

Furthermore, Ofcom proposes that the relevant wholesale markets should include all the substitutable access products which are required to secure effective and ongoing competition at the retail level. In this regard, Ofcom notes that BT's GPON¹⁴-based fibre network is at an early stage of development and that widespread GPON unbundling is likely to be too costly and impractical from an economic perspective, at least in the immediate term¹⁵. Ofcom concludes that other types of virtual local access, with features similar to physical unbundling, should be included in the market for wholesale local access.

On the basis of the substitution analysis and the need to secure adequate competition on the retail broadband markets, Ofcom proposes to include in the wholesale local access market a virtual unbundled local access (VULA) product. Openreach has been developing a set of Generic Ethernet Access (GEA) products which would form the basis of VULA¹⁶. Ofcom explains that although VULA is a product which includes active electronic equipment and provides virtual, bitstream-type access, its main features render it similar to products included in the market for local physical access. The key characteristics for VULA are: Local (interconnection should occur locally); Service-agnostic (should be able to support a multitude of services); Uncontended (dedicated capacity should be available to the end-user); Control of access (sufficient control of the access connection should be available); and Control of customer premises equipment (CPE) (sufficient control of CPE should be available).

Ofcom proposes to define two geographic WLA markets: (i) the UK excluding the Hull area and (ii) the Hull area.

II.2.2. Wholesale broadband access

Ofcom defines the WBA market as asymmetric broadband access and any backhaul which is necessary to allow interconnection with other CPs, which provides an always-on capability, allows both voice and data services to be used simultaneously and provides data at speeds faster than a dial-up connection. Ofcom also proposes to include, as substitutable products, fibre-based, cable-based and LLU-based services. The latter two products are included in the market on the basis of indirect constraints, relying on the evidence available from previous reviews. This market includes both business and residential customers.

¹² The product should not be confined to supporting particular downstream services.

¹³ The capacity in the access segment (from the premises to the point of interconnection) should be dedicated to the end-user, as in the case of LLU.

¹⁴ Gigabit Passive Optical Network.

¹⁵ There is likely to be a high number of passive splitter locations where access must be granted to connect a relatively low number of households and the process for disconnecting/reconnecting end-user fibres will require significant manual intervention.

¹⁶ In order to fulfil the requirements for VULA, the GEA products need to be adapted. In particular, Ofcom explains that: (i) BT would need to ensure that a stand-alone version of its FTTC GEA products is made available (i.e. not tied to another BT product or service); and (ii) in the event that BT were to choose to embed an analogue terminal adaptor (ATA) in the network terminating equipment, the voice function and associated control functions should be available at the local serving exchange and not extended beyond it. In addition, Ofcom explains that further consultations will be held with the industry regarding the design of a GEA multi-port master device for use on customers' premises.

Ofcom maintains¹⁷ its view that wholesale broadband access services should be divided into the following relevant geographic markets:

- the Hull area: where only KCOM is present;
- market 1: local exchanges where only BT is present;
- market 2: local exchanges with two or three principal operators¹⁸ (present or forecast);
- market 3: local exchanges with four or more principal operators (present or forecast).

II.3. Finding of significant market power

II.3.1. Wholesale local access

Following its analysis of the market for wholesale local access services, Ofcom concluded that BT has SMP in the UK, excluding the Hull area, and that KCOM should be designated as SMP operator in the Hull area. With regard to BT's SMP position, Ofcom analysed the following main criteria: (i) high and stable market shares¹⁹; (ii) barriers to entry; and (iii) countervailing buying power. As far as KCOM is concerned, the following criteria were analysed: (i) 100% market share; (ii) barriers to entry; and (iii) countervailing buying power.

II.3.2. Wholesale broadband access

Following the approach taken in its second review of this market, Ofcom concludes that there is no SMP on market 3²⁰. Furthermore, BT is considered to have SMP on markets 1 and 2 and KCOM is found to have SMP in the Hull area. The SMP assessment is based on: (i) market growth and market shares taking into account self-supply by cable and LLU operators; (ii) future potential market shares; (iii) barriers to entry and expansion; (iv) economies of scale and scope; and (v) countervailing buying power. In volume terms, Ofcom estimated that BT accounted for 28.5% of market 3 (compared with about 38% in the previous market review). On markets 1 and 2, BT is considered to have market shares of 98.5% and 69% respectively. KCOM has a 100% share of the market in the Hull area.

¹⁷ Ofcom proposes to keep the same criteria for defining the geographic market as used in the previous market review except for one minor change. It now proposes to remove the threshold for exchanges with fewer than 10 000 premises. Where these exchanges are forecast to have four or more operators that provide broadband services over their own access networks or LLU operators (but currently have fewer than four), they will be included in market 3.

¹⁸ Ofcom uses the criteria defined in the previous market review to identify the principal operators (see footnote 7). However, the 10% coverage threshold required for LLU operators is no longer applied. For the purposes of the review, Ofcom identified the following LLU principal operators: Talk Talk, Sky, Orange, O2 and Cable & Wireless Access.

¹⁹ According to Ofcom, BT's market share in 2009 was 84%.

²⁰ Based on volumes in September 2009 and forecasts made from information supplied by operators, market 3 comprises 1 287 local exchanges and accounts for 71.8% of UK delivery points (excluding the Hull area).

II.4. Regulatory remedies²¹

II.4.1. Wholesale local access

Ofcom proposes to impose the following obligations on both KCOM and BT: (i) general network access; (ii) requirement not to discriminate unduly; (iii) price control based on an LRIC+ method; (iv) transparency requirements²²; and (v) cost accounting and accounting separation.

Furthermore, Ofcom proposes specifically to impose on BT the requirement to provide local loop unbundling (LLU) services (including shared access) and, in the case of the NGA networks, the requirements to provide (i) virtual unbundled local access (VULA); (ii) sub-loop unbundling (SLU); and (iii) physical infrastructure access (PIA) consisting of duct and pole access.

Regarding LLU, Ofcom proposes to maintain the charge control obligation which it had previously imposed in 'A new pricing framework for Openreach'.

In addition, Ofcom proposes that BT should price PIA and SLU at their long-run incremental cost (LRIC), allowing a mark-up for common cost recovery. The proposed SMP condition on PIA should allow an 'appropriate' risk premium to be reflected in BT's charges. The proposed condition would cover both old and new duct and pole infrastructure, although the definition of 'appropriate' risk premium would differ between them.

In the case of the VULA service, Ofcom would like to allow pricing flexibility, e.g. geographic variations, volume discounts and tiered pricing. However, BT is required to provide VULA to CPs on an equivalence of input (EoI) basis, i.e. on the same timescales, terms and conditions (including price and service levels), by means of the same systems and processes and by providing the same information as to its own downstream divisions.

II.4.2. Wholesale broadband access

With regard to markets 1 and 2, Ofcom proposes to impose on BT the following obligations: (i) requirement to provide network access on reasonable request; (ii) requirement not to discriminate unduly; (iii) requirement to publish a reference offer; (iv) requirement to notify charges, terms and conditions; (v) transparency as regards quality of service; (vi) requirement to notify technical information; (vii) accounting separation; (viii) cost orientation; and (ix) cost accounting. In addition, Ofcom proposes to impose on BT a charge control obligation on market 1.

In the Hull area, KCOM should comply with: (i) the requirement to provide network access on reasonable request; (ii) the requirement not to discriminate unduly; (iii) the requirement to publish a reference offer; (iv) the requirement to notify charges, terms and conditions; (v) transparency as regards quality of service; (vi) the requirement to notify technical information; and (vii) accounting separation.

²¹ 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.

²² Requirement to publish a reference offer, requirement to notify charges, terms and conditions, requirement to notify technical information and transparency as regards quality of service.

III. COMMENTS

On the basis of the present notifications and the additional information provided by Ofcom, the Commission has the following comments²³:

Market for wholesale local access

Inclusion of a virtual unbundled local access product in the WLA market and implementation of VULA under the legally binding undertakings

The Commission takes note of the substitutability test provided by Ofcom, according to which VULA — as a local, service-agnostic, uncontended product, which ensures sufficient control of the access connection and control of customer premises equipment — should be included in market 4 in the Recommendation. In particular, although VULA is characterised as an active NGA product, it has many features which indicate that, in terms of functions, it is equivalent to local loop unbundling. Moreover, the level of control of the access connection and of the end-user connection provided by the VULA service appears significantly different from the level of control offered by other virtual access products. In particular, VULA should be made available at a location close to the end customers' premises, similar to LLU. Furthermore, it should allow product differentiation and innovation similar to LLU and thus give access-seekers a sufficient degree of control, including the quality of service, over the local connection to the end-user, even if it does not give the alternative operator the same freedom to offer retail products as those he could offer through a fully unbundled fibre line. All these features distinguish VULA from bitstream access products, whether regional or national. The Commission consequently does not contest, in the present case, that the local, service agnostic and un-contended nature of this particular service and the level of control granted by such a product could justify its inclusion in Market 4. However, the Commission invites Ofcom to monitor development of the VULA product and use of the product by CPs and to ensure that VULA is fully implemented with the above-mentioned characteristics.

Moreover, the Commission notes that VULA is based on BT's GEA products, which are developed by Openreach and subject to EoI requirements stemming from the Undertakings agreed between Ofcom and BT. The Commission therefore understands that the key characteristics of the products rest on adaptation by BT of its GEA products, in particular to offer the interconnecting CP a high level of control of the access connection and of the end-user connection. Consequently, in cases where variations of existing products must be implemented, the Commission calls on Ofcom to ensure that those fulfil all the VULA's functional characteristics.

In addition, the Commission would express the view that legally binding undertakings offered by the incumbent operator to the NRA and formally accepted by the latter, pursuant to their responsibilities under telecommunications law — insofar as they are aimed at enforcement of regulatory obligations and amend or replace existing regulatory obligations — must be considered directly related and/or ancillary to those regulatory obligations. As such, legally binding

²³ In accordance with Article 7(3) of the Framework Directive.

undertakings constitute regulatory obligations and must therefore be subject, at the draft stage, to consultation at both national and Community levels before they are adopted in order to secure the transparency of the process and adequate involvement of all interested stakeholders, i.e. the Commission and other NRAs.

Inclusion of cable in the WLA market on the basis of indirect constraints

Firstly, the Commission would stress that — to its knowledge — the unbundling of cable networks does not at this stage appear technologically possible or economically viable, thus ruling out the possibility of direct wholesale substitution between cable lines and copper loops. Despite this fact, unlike other NRAs, Ofcom nonetheless intends to include cable in the WLA market on the basis of indirect constraints.

According to Ofcom, the hypothetical monopolist test (HMT) analysis of indirect constraints involves assessing the extent of demand-side and supply-side substitution between loop-based and cable-based services, where cable services are available. Under the assumptions of the HMT framework, an increase in the price of the (notional) WLA would be passed on to the corresponding retail access prices paid by customers. The extent to which retail prices would increase would depend on the proportion of the retail price made up by the price of the wholesale input. Ofcom estimated this to be between 65 % and 75 %.

The Commission is concerned that Ofcom has not provided sufficient justification as to why any price increase would be entirely passed on to the end-users of retail broadband access products or that sufficient demand substitution would take place at retail level to render that price increase unprofitable, in particular because an LLU price increase could also affect other retail products, such as voice telephony and IPTV. Moreover, it is doubtful that competitors would not be able at least partly to absorb a 10% price increase in their margins. Incomplete pass-through of this price increase would further weaken the substitution effect at the retail level.

For these reasons, the Commission takes the view that cable should not be included in the market definition, as its inclusion would lead to overstatement of the competitive constraints on LLU. As previously stated by the Commission, where pricing constraints from the retail market are found to exist, they should be taken into account at the stage of the SMP assessment. However, as Ofcom admits itself, inclusion of cable could affect the SMP conclusions only if an operator were found not to hold SMP on the broader market. As BT was found to hold SMP, even assuming a broader market definition, inclusion of cable hence makes no difference to the outcome of this market review. For this reason the Commission does not challenge Ofcom's finding, but urges the British regulator not to include cable in the WLA market in its final measure.

Choice of proportionate and justified access remedies

The Commission notes that Ofcom does not impose fibre unbundling, given that it is unlikely to be cost-effective in the UK due to BT's network GPON topology, which could result in a low level of aggregation of households served. On the basis of the evidence provided, the Commission does not challenge the finding that today fibre unbundling would not be a justified and proportionate remedy and agrees that VULA, which offers characteristics that appear comparable to

fibre unbundling, allows competitive entry on the WLA market²⁴. In addition, the Commission notes that alternative operators can also rely on the SLU and the PIA remedies to climb the ladder of investment and roll out their own fibre lines closer to their customers' premises. However, in the context of NGA developments, NRAs should, as a matter of principle, require unbundled access to the fibre loop irrespective of the network architecture implemented by the SMP operator. In this respect, in line with the required forward-looking approach, the Commission invites Ofcom to assess whether GPON unbundling could be cost-effective, particularly if BT undertakes selective deployment in densely populated areas where sufficient aggregation could be achieved.

Furthermore, the Commission invites Ofcom to re-assess the proposed remedies as soon as the technology enabling fibre unbundling (e.g. WDM²⁵) is available. In this respect, the Commission would stress that a VULA remedy should be considered as a transitional measure. In the long run, fibre unbundling will allow full and direct control over the end-users (also allowing to offer retail products improved compared to those offered by the access provider through an unbundled fibre line) and provide the next rung on the ladder of investment. Accordingly, the VULA remedy should be replaced by fibre unbundling as soon as it is technically and economically feasible or should possibly continue to be required in addition to full fibre unbundling. Consequently, considering the transitional nature of the VULA product, the Commission expresses concerns about the timeframe for the review of the market definition and remedies, i.e. four years after adoption of the notified draft remedies. Instead, Ofcom should, in this particular case, review within a shorter period of time whether its market definition and proposed remedies are in line with competition law principles (i.e. whether there is a possibility of providing unbundled access to the fibre infrastructure). The Commission would also point to the fact that, pursuant to Article 16(6) of the Framework Directive, as amended by Directive 2009/140/EC²⁶, 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.

Lack of price control to be imposed for VULA

The Commission takes note of Ofcom's proposal to allow significant pricing flexibility for VULA (e.g. regarding geographic variations, volume discounts or

²⁴ See also recital 60 of 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 and services (the 'Better Regulation Directive'), which states that 'in circumstances where unbundled access to local loop or sub-loop is not technically or economically feasible, relevant obligations for the provision of non-physical or virtual network access offering equivalent functionality may apply'.

²⁵ Wavelength Division Multiplexing.

²⁶ 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 and services (the 'Better Regulation Directive'), OJ L 337, 28.12.2009, p. 37.

tiered pricing), given the uncertainties surrounding the forecasts for demand, costs and revenue and the constraints from current generation broadband subject to price control, from competition from cable operators at the retail level and from other cost-oriented physical remedies (e.g. PIA and SLU). Furthermore, Ofcom explains that any pricing adopted by BT would need to be fair and non-discriminatory and that strict interpretation of ‘no undue discrimination’ under the EoI requirements should adequately prevent BT from favouring its downstream divisions. However, the Commission would recall that, as a general rule, access prices need to be cost-oriented. In accordance with the regulatory framework, such prices can be appropriately adjusted for investment risk, according to the specific contractual setting, in order to drive both competition and investment in NGAs. Hence, the price of access to unbundled fibre loop should, in principle, be cost-oriented, taking into account any additional and quantifiable investment risk incurred by the SMP operator.

Migration process in an NGA context

The Commission notes that Ofcom’s notification has not considered detailed obligations relating to the migration from copper to fibre loops, in particular in the context of the lower number of main distribution frames (MDFs) required to provide broadband services. The Commission would recall that migration from copper to fibre loops and the dismantling of exchanges could substantially affect the business case for alternative operators. It is therefore critical that CPs obtain all relevant information from the SMP operator concerning any planned alterations to the network, particularly when the SMP operator envisages replacing part of its existing copper access network with fibre and plans to decommission currently used interconnection points. The Commission therefore invites Ofcom to include, as part of the transparency obligation, a requirement for BT to put forward a migration procedure for alternative operators in the event of planned changes in BT’s network topology.

Remedies imposed in the context of NGA development and need for a consistent European approach

The Commission welcomes the fact that Ofcom has included fibre access networks and fibre-based services in both relevant markets. This approach is expected to contribute significantly to development of NGA infrastructure-based competition in the UK.

In this context, the Commission would highlight that it is necessary to provide further guidance in the context of the NGA roll-out in order to ensure legal certainty for investors and to prevent undesirable divergences of regulatory approaches on the internal market. To this end, the Commission is working towards a Recommendation on NGA remedies in order to ensure a consistent regulatory approach to the relevant networks across the EU. In the light of this, the Commission invites Ofcom to revisit its analysis when it carries out its next review of wholesale broadband markets, along the lines of this Recommendation, once adopted.

Market for wholesale broadband access

Inclusion of self-supply in market 5 on the basis of indirect constraints

Ofcom bases its inclusion of cable- and LLU-based WBA services in the relevant

market on indirect constraints stemming from the underlying retail markets.

The Commission has noted in the past that competition at the retail level from vertically integrated undertakings may be such as to exert an indirect constraint on the market for wholesale access services and that, where such indirect pricing constraints are found to exist, they should be taken into account in the SMP assessment. As already underlined by the Commission in previous cases, it is essential that the strength of the constraints posed by vertically integrated companies should be correctly reflected in the assessment and the Commission has set out appropriate criteria against which the nature of such indirect substitution effects may be assessed²⁷.

In response to the arguments put forward by Ofcom in this respect, the Commission would highlight that Ofcom has not provided sufficient evidence that a price increase would be entirely passed on to the end-users of retail broadband access products and that competitors would not be able at least partly to absorb this price increase in their margins.

The Commission notes that Ofcom takes indirect constraints into account in its market definition only for exchange areas where Ofcom considers their presence capable of exercising a sufficient competitive constraint. Thus, in view of this approach, even if indirect constraints were taken into account in the market power assessment rather than at the market definition stage, this would not have led to a significantly different outcome than the one currently proposed by Ofcom²⁸. The Commission therefore considers that, since a conclusion on whether such constraints should be taken into account in the definition of the relevant market or in the SMP assessment is not relevant to the regulatory outcome, this question could be left open at present.

Criteria used for the geographic differentiation of the wholesale broadband access market

The Commission would reiterate its comments in case UK/2008/0733 regarding definition of sub-national markets for wholesale broadband access. The Commission's view remains valid, i.e. that a geographic delineation which is based primarily on the number of operators present in a local exchange is not, in itself, sufficiently detailed or robust to identify real differences in competitive conditions for the purposes of the market definition. In assessing whether conditions of competition within a geographic area are *similar* or *sufficiently homogeneous*, additional structural and behavioural evidence is necessary.

²⁷ Explanatory Note to the Commission Recommendation 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 (C(2007) 5406), pp. 34-35. See also cases UK/2003/0032, NL/2005/0281, AT/2005/0312 and UK/2007/0733.

²⁸ In that regard, while the number of operators and their market shares at a given exchange might have been different had cable and/or LLU not been included at the market definition stage and this could have resulted in a different geographic segmentation of the market, the constraint posed by cable and LLU in local exchange areas would nonetheless need to have been factored into the SMP analysis. Furthermore, Ofcom indicates that most of the large LLU operators are either already selling wholesale services to third parties (albeit low volumes) or planning to do so in the near future. In its response to the request for information, Ofcom also indicates that there are no obvious constraints to LLU operators increasing their provision of wholesale services.

Relevant evidence would include information on the distribution of market shares and the evolution of shares over time. In addition, evidence of differentiated retail or wholesale pricing which might apply could help indicate different regional or local competitive pressures. It is also considered appropriate to look at the pricing of both the incumbent and alternative operators and at its evolution over time in the relevant areas.

The position set out above can be important in the context of mergers and acquisitions which lowered the number of competitors on markets defined by Ofcom. Application of the number of operators as the sole criterion for SMP assessment could therefore lead to incorrect conclusions about the state of competition and scope of regulation.

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/EC²⁹ 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 Commission³⁰ 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 publication³¹. You should give reasons for any such request.

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

²⁹ 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.

³⁰ Your request should be sent either by email: INFSO-COMP-ARTICLE7@ec.europa.eu or by fax: +32 2 298 87 82.

³¹ The Commission may inform the public of the result of its assessment before the end of this three-day period.