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Rundfunk und Telekom
Regulierungs-GmbH (RTR)

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Austria

For the attention of:
Mr. Georg Serentschy
Geschäfsführer

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Dear Mr Serentschy

Subject: Commission decision concerning Case AT/2013/1442: Wholesale terminating segments of leased lines in Austria

Opening of Phase II investigation pursuant to Article 7 of Directive 2002/21/EC as amended by Directive 2009/140/EC

Comment pursuant to Article 7(3) of Directive 2002/21/EC

Commission decision concerning Case AT/ 2013/1443: Retail market for leased lines up to and including 2 Mbit/s in Austria

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

I. PROCEDURE

On 3 April 2013, the Commission registered a notification from the Austrian national regulatory authority, Rundfunk und Telekom Regulierungs-GmbH (RTR)[1], concerning retail market for leased lines up to and including 2 Mbit/s[2] and the wholesale terminating segments of leased lines in Austria[3].

1 Under Article 7 of 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 market 7 in Commission Recommendation 2003/311/EC on relevant product and service markets replaced by Commission Recommendation 2007/879/EC.

3 Corresponding to market 6 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.

The national consultation[4] ran from 22 January to 1 March 2013.

On 11 April 2013, a request for information (RFI)[5] was sent to RTR and a response was received on 16 April 2013. Additional information was also provided by RTR on 22 April 2013.

Pursuant to Article 7(4) of the Framework Directive, the Commission may notify the national regulatory authority (NRA) and the Body of European Regulators for Electronic Communications (BEREC) of its reasons that the draft measure would create a barrier to the internal market or its serious doubts as to its compatibility with EU law.

II. DESCRIPTION OF THE DRAFT MEASURE

II.1. Background

The previous third round market analysis was made in various steps.

In 2008, the market definition[6] both of the retail and the wholesale leased lines was notified to and assessed by the Commission under cases AT/2008/0838[7] and AT/2008/0836[8] respectively.

With regard to the retail market, RTR defined a national market for leased lines with a bandwidth of up to and including 2 Mbit/s and concluded that it met the three criteria test and was therefore susceptible to ex-ante regulation. The Commission invited RTR to reconsider the effectiveness of wholesale remedies when carrying out the full market analysis and to amend the remedies if necessary.

With regard to wholesale terminating segments of leased lines, RTR distinguished between three segments (low, high and very high bandwidths)[9] and concluded that only the low and high capacity segments should be subject to *ex ante* regulation. Furthermore, in the high bandwidth RTR claimed a geographical segmentation and excluded 12 cities[10] from ex-ante regulation. In its comments, the Commission commented on the geographical delineation of the high bandwidth segment urging RTR to provide additional evidence with regard to the heterogeneity of competitive conditions in different regions identified when submitting its notification on the full market analysis and also pointed out that it reserved its rights, when assessing the subsequent notified draft market analysis, to examine whether the then notified market definition still reflected market reality.

4 In accordance with Article 6 of the Framework Directive.

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

6 RTR defined leased lines as facilities without on-demand switching functionality which provide transparent transmission capacity between two network termination points located in Austria in a symmetrical and a bidirectional manner.

7 C(2008) 8848

8 C(2008) 8848

9 Market for low bandwidth (up to and including 2Mbit/s), market for high bandwidth (greater than 2Mbit/s up to 155 Mbit/s) and market for very high bandwidth (greater than 155Mbit/s).

10 Vienna, Linz, Graz, Salzburg, Innsbruck, Wels, Feldkirch, Steyr, Klagenfurt, Dornbirn, Bregenz and Hallein were grouped in the so-called 'Area 1' whereas the rest of Austria was referred to as 'Area 2'.

In February 2010[11], the SMP and related obligations for the market for terminating segments of leased lines with low bandwidths (up to 2 Mbit/s) and those for high bandwidths in Area 2 that were defined in 2008, were notified to and assessed by the Commission under cases AT/2010/1048[12] and AT/2010/1049 respectively. While the latter notification was withdrawn during the Phase I investigation, RTR designated Telekom Austria as having SMP and proposed to impose a full set of remedies in the low bandwidth segment. It its comments the Commission invited RTR to ensure that the price control regime applied in the final measure would take due account of productivity progress.

Finally, in July 2010, the SMP findings and remedies to be applied to the retail market for leased lines up to and including 2 Mbit/s defined in 2008 were notified to and assessed by the Commission under case AT/2010/1107[13]. RTR designated A1 Austria Telekom as having SMP and proposed a full set of remedies. The Commission commented on the risks of notifying the market definition in advance of the full market analysis and remedies, and asked RTR to examine by way of a thorough substitutability analysis at the latest in the next round market review whether Ethernet services are part of the relevant retail market and to carry out a coordinated and simultaneous analysis of the wholesale and retail markets and submit a complete new analysis before the end 2012.

II.2. Current draft measure

II.2.1 Market definition

RTR defines leased lines, both at retail and wholesale level, as facilities that provide transparent transmission capacity between two network termination points located in Austria in a symmetrical and bidirectional manner and which do not have a switching function.

II.2.1.1 Retail leased lines

The product market definition consists of retail leased lines of any bandwidth[14] and includes traditional interface, both analogue with adequate bandwidth for basic-or high-quality voice, and 64 or 2048 kbit/s digital leased lines, as well as leased lines with end-user Ethernet interfaces.

The relevant geographic market is national.

II.2.1.2 Wholesale Terminating segments of leased lines

The product market definition includes terminating segments of leased lines with traditional interfaces for all bandwidths, terminating segments of Ethernet services[15] with

11 In 2009 RTR also notified the withdrawal of the regulatory obligations imposed on Telekom Austria in the second round of market analysis under case number AT/2006/0508 in the wholesale market for terminating segments of leased lines for very high bandwidths and in the wholesale market for leased lines with high bandwidths in Area 1. At that time, the Commission invited RTR to closely monitor market developments and the evolution of the competitive conditions, and to assess in the next notification if the boundaries chosen for the two geographic markets should remain.

12 C(2010) 1789

13 C(2010) 5752

14 In its reply to the RFI, RTR clarified that the market definition includes all bandwidth categories and that the term 'market for retail leased lines up to and including 2 Mbit/s' is explained by the currently (regulated) retail market which included only bandwidths up to 2 Mbit/s.

15 There are 25 providers of leased lines in Austria, 13 of which offer Ethernet with guaranteed bandwidth. The demand for Ethernet services, although lower than for leased lines, is showing strong

guaranteed bandwidth for all bandwidths, and terminating segments for dark fibre. The market concerned also includes self-supplied services[16].

RTR states that there is a substitution chain that justifies the inclusion of all bandwidth categories[17] in the market.

According to RTR, the number of high bandwidth terminating segments of leased lines based on Ethernet services has increased continuously in recent years and will continue to grow (mainly due to LTE/NGA expansion).

RTR also includes dark fibre in the market definition[18]. RTR argues in this respect that despite a significant demand for dark fibre, there is still no nationwide offer. According to RTR, the sole provider of a national comprehensive network of dark fibre, A1 TA, provides dark fibre to its own mobile branch and has strong incentives to actively refuse access to other mobile telephony companies and providers on the leased line market[19]. In RTR's view this puts competitors at a disadvantage in the market and could undermine the expansion of high-speed technologies in Austria.

With regard to the relation of prices between leased lines and dark fibre, RTR states that Ethernet services are several times (up to 10 times) more expensive than dark fibre (without necessary equipment costs to activate the line). According to RTR, Austrian operators already use dark fibre (instead of leased lines/Ethernet services of higher bandwidths) whenever possible.

The relevant geographic market for wholesale terminating segments of leased lines is national[20].

II.2.2 Finding of significant market power

II.2.2.1 Retail leased lines up to and including 2 Mbit/s

Since the retail market is no longer listed in the Recommendation on Relevant Markets, RTR

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growth. According to RTR, between 2008 and 2010 the demand for terminating segments of leased lines decreased by 7.500 lines, while the demand for Ethernet services increased by 7.000 lines. 10 out of 15 companies questioned regarded Ethernet as a viable alternative to traditional leased lines.

16 According to RTR, self-supply must be included based on the assumption that the internal traffic would be made available on the merchant market in case of an increase or decrease of market prices.

17 RTR found that the differences between bandwidths of e.g., 64 kbit/s, nx64 kbit/s, 2 Mbit/s, 34 Mbit/s, and 150 Mbit/s are sufficiently small so that the price of any given bandwidth is influenced by the price of the neighbouring one.

18 So far, The Austrian Telecommunications Act 2003 allows consumers the right of joint use in relation to dark fibre in order to make individual point-to-point connections. According to RTR, these procedures which are directed to A1 TA, regional energy suppliers and the Austrian Federal Railways, are considered today unsuitable for extensive rural development and will be replaced by the access to dark fibre obligation.

19 According to operators such as Hutchison 3G Austria GmbH (whose position has been submitted with the notification) and Orange Telecommunication GmbH, a refusal to provide dark fibre has already taken place. They consider that by securing efficient access to dark fibre in the medium and long term is important in the context of the roll-out of the 4G mobile telephony infrastructure. This position is shared by VAT (Association of Alternative Telecom Network Operators) and ISPA (Internet Service Providers Austria).

20 According to RTR, terminating segments are offered and requested nationwide in similar competitive conditions. Market shares although slightly different in some municipalities compared to the rest of Austria exceeds in any case 70% (including self-supply) and there are no sufficiently large differences in prices at geographic level to warrant different geographical markets.

carried out the three-criteria test and observed the following: (i) declining market share of the SMP operator, (ii) considerable decline in the demand for leased lines of less than 2 Mbit/s, (iii) increased replacement of low bandwidth lines with higher-bandwidth leased lines, (iv) presence of high competitive pressure from the adjacent market for broadband internet.

Based on those observations, RTR concludes that the second relevant criterion (the existence of a market structure that does not tend towards effective competition) and the third criterion (insufficiency of general competition law) are not fulfilled and that this market is no longer relevant for ex-ante regulation.

II.2.2.2 Wholesale Terminating segments of leased lines

RTR proposes to designate A1 TA as the undertaking having SMP in the wholesale terminating segment of leased lines market.

The main criteria considered by RTR when reaching its conclusion are (i) high market shares (ii) presence of high and non-transitory barriers to market entry[21], (iii) vertical integration and incentives to leverage its market power both horizontally and vertically, (iv) control of infrastructure not easily duplicated[22], (v) absence of countervailing buyer power, (vi) product differentiation, (vii) pricing behaviour[23], and (viii) denial of access (dark fibre).

As regards the market shares, RTR presents national market shares including self-supply. According to this analysis A1 TA has high and stable market shares (82% in terms of number or leased lines, 63% in terms of weighed capacity).

In its response to the RFI, RTR presents market shares at national level[24] in the merchant market at the level of around 40% (turnover) and 20% (in terms of bandwidth). A1 TA's market shares broken down by different bandwidths show levels of around 60 to 80% in low capacity segments and 35 to 55 % in high capacity when including self-supply. In the merchant market, A1 TA's market shares are lower in the high bandwidth and range around 5%-15%.

II.2.3 Regulatory remedies

II.2.3.1 Retail leased lines up to and including 2 Mbit/s

RTR proposes to repeal all obligations imposed on A1 TA pursuant to the last market analysis.

II.2.3.2 Wholesale Terminating segments of leased lines

RTR intends to impose the following regulatory obligations on A1 TA:

- Access to all required infrastructure elements and services (i.e. colocation) as well as ancillary services necessary for the access to terminating segments of leased

21 Economies of scale and sunk costs caused mainly by digging cost and economies of scope due to the variety of products offered by the SMP operator are structural barriers. Line rights over third-party land and digging-up prohibitions imposed by territorial entities are legal barriers to market entry. Availability of frequencies, restrictions on maximum bandwidths and dependence on weather and topographical restrictions constitute technical barriers.

22 A1 TA has a crucial advantage over other suppliers, which mostly only have their own infrastructure in a particular region or city but have no nationwide fibre optic infrastructure. Moreover, A1 TA holds more than 70% of the network termination points in 90% of the 73 town-rate municipalities.

23 On average A1 TA consistently charges higher fees and still enjoys the largest market share.

24 Covering capacities up to 155 Mbit/s.

lines, Ethernet services and dark fibre (with specific limitations[25]) regardless of the purpose of use;

- Price-cap regulation concerning access to terminating segments of leased lines and Ethernet services and widely cost oriented tariffs for access to terminating segments of dark fibre;
- Non-discrimination obligation including the obligation to publish detailed reference offers on the undertaking's webpage and the obligation to keep the offers up to date and inform of any changes;
- Transparency obligation concerning the location of available dark fibre infrastructure differentiated by the geographical area of the request;
- Obligation to publish key performance indicators quarterly;
- Obligation to keep accounting separation.

III. ASSESSMENT

III.1 Retail leased lines up to and including 2 Mbit/s

The Commission has examined the notification and have no comments.

III. 2. Wholesale Terminating segments of leased lines

The Commission has examined the notification and the additional information provided by RTR and would like to comment on the following issue:

Inclusion of dark fibre in the product market definition

As defined in the Recommendation of Relevant Markets, the key features in the demand for and supply of dedicated connections are service guarantees, bandwidth distance and the location or locations to be served.

With a view to delineating the boundaries of the market, several factors should be taken into account (i.e. different product functionalities and intended use, price evolution over time, cross-price elasticity).

RTR proposes to include dark fibre access lines in the market for terminating segments of leased lines. Whereas recognising that dark fibre based connections could also be capable of providing dedicated capacity, the Commission believes that from a functional viewpoint, access to dark fibre tends to be only partially substitutable with terminating segments of leased lines. In view of the Commission, customers would not switch from a complete connection which immediately ensures dedicated, guaranteed capacity to a dark fibre connection, as the latter would still need to be activated by additional equipment. Moreover, the functional differences tend to be reflected in additional cost related to the activation of dark fibre lines.

In its notification RTR provides some analysis based on competition law principles that would justify such a broad market definition. In particular, in its response to the RFI, RTR compares only prices for access to Ethernet-based leased lines and dark fibre lines without taking into account equipment costs. On

[25] These access requirements only apply with respect to dark fibre to infrastructure that already exists at the time of demand for which A1 TA still retains a technical operational reserve of two fibres (one fibre pair).

the basis of this analysis RTR concludes that the prices for Ethernet based leased lines are several times higher than access to dark fibre (without equipment). On top of that Austrian operators claim that they use dark fibre (instead of leased lines / Ethernet services of higher bandwidths) whenever possible. The Commission would like to emphasize that in order to verify whether customers purchasing terminating segments of leased lines would switch to dark fibre (bearing in mind total costs related to the usage of this infrastructure) in case of a small but significant (5 to 10%) increase of prices for terminating segments of leased lines by the hypothetical monopolist, RTR should have analysed total costs of both services. The Commission however takes note of the national circumstances in Austria, where according to RTR (i) mobile broadband services play a significant role and (ii) dark fibre-based services are already used as one of the key products (in particular by mobile operators) in a similar way as terminating segments of leased lines.

Against this background, the Commission does not object to RTR's proposal to include dark fibre in the product market definition; however they would like to invite RTR to closely monitor the market and observe whether dark fibre and leased lines services would evolve towards further substitutability or whether they turn out to be rather different, complementary services.

On the basis of the notification and the additional information provided by RTR, the Commission considers that RTR's draft measure falls within Article 7(4) of the Framework Directive and have serious doubts as to its compatibility with EU law for the following principal reasons:

Homogenous product market definition

Compliance with Article 8 (5) (a) to (c) and Article 15(3) of the Framework Directive

According to the Commission Guidelines on market analysis and the assessment of significant market power[26], the delineation of the relevant market should be based on a substitutability test comprising the analysis of competitive constraints arising from both demand and supply side. As explained above, the boundaries of a particular market must be established on the basis of a substitutability test that analyses product functionalities, intended use, price evolution, and cross-price elasticity. The inclusion/exclusion of the different products under consideration in the market leads respectively to a broader or narrower market definition, thus influencing the market shares calculation and the SMP assessment.

At this occasion, and contrary to the previous market review, RTR proposes to define a single wholesale product and geographic market for terminating segments of leased lines. However, on the basis of the limited information provided by RTR so far, the Commission came to the preliminary conclusion that competitive conditions are heterogeneous in the low and high capacity market segments (i.e. up to and including 2 Mbit/s and above 2 Mbit/s of bandwidth), and could justify a further delineation of markets according to bandwidth.

According to the data provided in the notification, the competitive position of A1 TA in the segment of high capacity terminating leased lines - where it only provides 40%-60% in terms of bandwidth (including self-supply) and below 20%

[26] Commission Guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications and services (2002/C 165/03)

in terms of bandwidth in the merchant market and where alternative operators apparently have invested and are still investing in their own infrastructure - differs significantly from those of low capacity terminating segments. In the latter A1 TA's market shares (including self-supply) range from 60% (below 2 Mbit/s) to 80% (2 Mbit/s) and from approximately 5% (lines below 2 Mbit/s) up to approximately 65% (lines of 2 Mbit/s) when self-supply is excluded.

The relatively low market shares of A1 TA for the high bandwidth suggest that the competitive conditions identified by RTR in its previous market review - where in some municipal areas high capacity leased lines were provided in competitive markets - remain unchanged. If this would be the case, the reintroduced regulation could hamper the presence of alternative operators in the market, who currently enjoy the flexibility of competing with the incumbents without any regulation in place. Moreover, it would also seem to suggest that entry barriers into a market for high bandwidth lines can be overcome, at least in some areas, and that alternative operators have been able to gain substantial market share bringing dynamics into the market. The Commission is concerned that reintroduction of regulatory remedies in those areas which are characterised by competitive conditions, could seriously damage business plans of alternative operators, who in order to remain competitive would then need to match the more attractive offers that would become available as a result of regulation.

In these circumstances, and in the absence of a sound substitutability analysis based on more detailed data, the Commission expresses serious doubts whether the draft measure complies with Article 8(5) (a) to (c) of the Framework Directives, in particular whether by way of the proposed measure RTR contributes to the development of the internal market by promoting regulatory predictability, ensuring that there is no discrimination in the treatment of undertakings and safeguarding competition and promoting infrastructure-based competition. Moreover the Commission has serious doubts whether the relevant product market has been delineated in accordance with the principles of competition law and therefore whether it complies with Article 15 (3) of the Framework Directive.

Insufficient market data supporting the designation of A1 TA as SMP operator at least in the high capacity segment of the market

Compliance with Article 8(5)c and Articles 14 to 16 of the Framework Directive

As explained in the Commission Guidelines on market analysis, markets must be defined and SMP assessed using the same methodologies and principles applied under competition law. In the Commission's decision making practice, single dominance concerns normally arise in the case of undertakings with market shares of over 40%, although the Commission may in some cases have concerns about dominance even with lower market shares, as dominance may occur without the existence of a large market share.

The Commission is of the view that so far RTR has not provided sufficient evidence on A1 TA's SMP in the market for wholesale terminating segments of leased lines.

RTR claims that self-supplied terminating segments of leased lines are included in the market based on the assumption that the internal traffic would be made available in the merchant market in case of an increase or decrease of market prices. However, the inclusion of so called 'captive sales' is not substantiated by any further analysis. In particular, RTR does not specify what kind of captive sales it takes into account (*i.e.* leased lines provided to the operator's subsidiaries for the purpose of further merchant sales at retail level or leased lines provided also for internal use of daughter companies) and how these sales affect A1 TA's market power in the merchant market for terminating segments of leased lines. The Commission acknowledges that some base stations of Austrian mobile operators could indeed be shared by more than one access seeker. This would then justify the inclusion of self- supplied terminating segments of leased lines, as the existing spare capacity could be used by more than one operator. However, RTR does not provide any evidence on the number of shared base stations but instead automatically includes all captively provided services in the calculation of market shares. This can artificially inflate the market shares of the vertically integrated operator.

Independently of the issue whether captive sales should be included in the relevant market or not, on the basis of RTR's analysis the Commission can conclude that A1 TA has high market shares only in the low bandwidth segments (i.e. up to and including 2 Mbit/s) whereas with respect to higher capacity terminating segments of leased lines, which seem to be, in line with RTR's findings, the most demanded product, A1 TA's market shares are much lower and range between 40%-60% when the self-supply is included and only around 5%-15% when only the merchant market is considered. The above-mentioned market shares seem to demonstrate that alternative operators have managed to gain a substantial part of the terminating segments of leased lines market in Austria, which suggests economic feasibility of the duplication of infrastructure at least in those areas where there is sufficient demand for high bandwidth leased lines products.

Against this background, the Commission is not convinced at this stage that the lack of duplicability of A1 TA's infrastructure would exist. The information available to the Commission does not support the conclusion that RTR has undertaken the assessment in accordance with Articles 14 to 16 of the Framework Directive, in particular with regard to Article 8(2) (b) of the Framework Directive. In these circumstances the Commission expresses its serious doubts about the designation of A1 TA as SMP operator in the high capacity segment of the market.

Creation of barriers to the internal market

The Commission concludes, at this stage, that RTR's draft decision would create a barrier to the development of the internal market. The finding of lack of competition at least for high capacity terminating segments of leased lines which contradicts RTR's previous assessment could carry considerably negative consequences for actually or potentially competing operators from other Member States who would intend to provide services in Austria.

Moreover, The Commission believes that the reintroduction of regulatory obligations in some densely populated areas of Austria where there was competition may lead to a situation where current competitors of A1 TA would be forced to compete with regulated services of the incumbent. The availability of regulated services in a market characterised by strong presence of alternative providers would negatively impact on the ability of the latters to offer services to their customers (including pan-European connectivity and other cross-border services) and would create distortions in the internal market.

In the light of the above, the Commission takes, at this stage, the view that the notified regulatory measure would therefore create a barrier within the single market.

The above assessment reflects the Commission's preliminary position on these particular notifications and is without prejudice to any position it may take *vis-à-vis* other notified draft measures.

The Commission points out that, in accordance with Article 7 of the Framework Directive, the draft measure on the wholesale terminating segments of leased lines in Austria shall not be adopted for a further two months.

Pursuant to Article 7(7) of the Framework Directive, RTR may adopt the draft measure concerning the retail market for leased lines up to and including 2 Mbit/s in Austria and, where it does so, shall communicate it to the Commission.

Pursuant to Recital 17 of Recommendation 2008/850/EC[27], the Commission will publish this document on its website, together with a notice inviting third parties to submit observations on this serious doubts letter within ten working days. The Commission does not consider the information contained herein to be confidential. You are invited to inform the Commission[28] within three working days following receipt whether you consider that, in accordance with European Union and national rules on business confidentiality, this document contains confidential information which you wish to have deleted prior to such publication. You should give reasons for such request.

Yours sincerely,
For the Commission
Neelie Kroes
Vice-President

[27] 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, OJ L 301, 12.11.2008, p. 23.

[28] Your request should be sent either by email: CNECT-ARTICLE7@ec.europa.eu or by fax: +32.2.298.87.82.