Wholesale call termination on individual public telephone networks provided at a fixed location

Identification and Analysis of Markets,
Determination of Market Power and Setting of Remedies

Response to Consultation and Final Decision

17th May 2010

Contents

Executive Summary

The Malta Communications Authority ("MCA") is hereby presenting its final decision on the markets for wholesale call termination on individual public telephone networks at a fixed location in Malta, following the notification of the draft decision to the EU Commission.

This document builds on a consultation exercise carried out by the MCA between the 14th of December 2009 and the 15th of February 2010, during which the MCA received one response to consultation from Vodafone (Malta) Ltd. This operator expressed agreement with the MCA's findings and conclusions put forward for consultation.

The MCA also consulted the Office for Fair Competition ("OFC") on the findings of this market review. From its investigations, the OFC agreed with such findings, and its official position is hereby being made available to the general public.

Background

The MCA published its first market review for wholesale call termination on individual public telephone networks at a fixed location in October 2005. Following the said consultation process, the MCA published its final decision which identified two relevant markets for wholesale call termination, namely:

- Wholesale call termination services provided by GO plc over its network; and
- Wholesale call termination services provided by Melita plc over its network.

Each identified market includes call termination services provided by the individual public telephone network operator to third party operators and also self-supplied termination.

Based on the evidence available, the MCA designated both GO plc and Melita plc with SMP in the provision of wholesale call termination services to third party operators over their own network. The main reasons justifying this decision were based on an analysis of three criteria namely market shares, the lack of countervailing buyer power and potential competition.

The MCA also noted that there are costs associated with the conveyance of calls between networks, with the operator hosting the called party expecting the originating operator to pay the network costs incurred to terminate the relevant call. In this regard, the MCA argued that, in the absence of regulation, fixed network operators ("FNOs") would be incentivised to set wholesale termination charges at above competitive levels. In these circumstances, suppliers of call termination would increase their revenues, whereas operators purchasing their service would either end-up with a lower profit margin or else consider feeding-through the increase in price of call termination on their retail call tariffs.

In view of the identified competition problems and the designation of SMP, the MCA imposed a set of obligations on both GO and Melita. The MCA imposed obligations of access, transparency, non-discrimination, cost orientation, cost accounting, and accounting separation on GO. On the other hand, the MCA imposed access, transparency, and non-discriminatory obligations on Melita. However, the MCA did not consider that there was a need to impose cost orientation, cost accounting and accounting separation obligations on Melita given that the operator was still a new entrant at the time. Instead the termination rate charged by this operator was pegged (at a maximum) to the rates set by GO (formerly known as Maltacom).

The current review

Identification of markets

The MCA defines five markets for wholesale fixed call termination on individual public telephone networks in Malta, namely:

- Wholesale fixed call termination services provided by GO plc over its network;
- Wholesale fixed call termination services provided by Melita plc over its network;
- Wholesale fixed call termination services provided by SKY Telecom Ltd over its SKYNet network;
- Wholesale fixed call termination services provided by Vodafone (Malta) Ltd over its network; and
- Wholesale fixed call termination services provided by Solutions and Infrastructure Services ("SIS") Ltd over its network.

The relevant geographic markets for the provision of wholesale fixed call termination on public telephone networks at a fixed location have been found to be national in scope.

Further details on the MCA's market definition exercise are found in Chapter 2 to this document.

Assessment of Significant Market Power ("SMP")

After having conducted an analysis of the relevant markets, the MCA is designating:

- GO plc with SMP in the market for wholesale fixed call termination provided over its own network;
- Melita plc with SMP in the market for wholesale fixed call termination provided over its own network;
- Vodafone (Malta) Ltd with SMP in the market for wholesale fixed call termination provided over its own network;
- SKY Telecom Ltd with SMP in the market for wholesale fixed call termination provided over its SKYNet network; and
- SIS Ltd with SMP in the market for wholesale fixed call termination provided over its own network.

In its analysis, the MCA took into account a selected number of criteria to justify the above, namely:

- market shares;
- entry deterrence and potential competition; and
- countervailing buyer power ("CBP").

Full details of the MCA's assessment of SMP are contained in Chapter 3 to this document.

Regulatory Implications

Given the position of dominance held by all SMP operators identified in this review, and in light of potential competition problems that may arise, the MCA deems it necessary to impose the following obligations on the said operators, namely:

a. Access to/and use of specific facilities;

b. Non-discrimination;

c. Transparency; and

d. Price control.

The MCA is also mandating the obligations of accounting separation and cost accounting on GO plc and Melita plc.

The MCA notes that its regulatory approach ensures that all remedial action is based on the nature of the competition problems that were identified, and that each obligation is proportionate and justified in light of the objectives set out in Article 4 of the Electronic Communications (Regulation) Act.

Full details of the MCA's regulatory approach, are contained in Chapter 4 to this document.

Chapter 1 - Introduction

1.0 The EU Regulatory Framework for Electronic Communications

The EU Regulatory Framework for Electronic Communications (also referred to as the eCommunications framework[1]) sets the ground rules for regulation and aims to ensure legislative stability and harmonisation of the regulatory approach across EU Member States.

The eCommunications Framework comprises of five directives as follows:

- Directive 2002/21/EC on a common regulatory framework for electronic communications networks and services ("the Framework Directive");
- Directive 2002/19/EC on access to, and interconnection of, electronic communications networks and associated facilities ("the Access Directive");
- Directive 2002/20/EC on the authorisation of electronic communications networks and services ("the Authorisation Directive");
- Directive 2002/22/EC on universal service and users' rights relating to electronic communications networks and services ("the Universal Service Directive"); and
- Directive 2002/58/EC concerning the processing of personal data and the protection of privacy in the electronic communications sector ("the Privacy Directive").

The Framework Directive provides the overall structure for the regulatory regime and sets out fundamental rules and objectives reading across all the directives. Article 8 of the Framework Directive sets out three key policy objectives namely the promotion of competition, the development of the internal market, and the promotion of the interests of the citizens of the European Union.

The Authorisation Directive establishes a system whereby any person will be generally authorised to provide electronic communications services and/or networks without prior approval. The general authorisation replaces the former licensing regime.

The Universal Service Directive defines a basic set of services that must be provided to end-users. The Access and Interconnection Directive sets out the terms on which providers may access each others' networks and services with a view to providing publicly available electronic communications services.

The above-mentioned directives were transposed into national legislation when the Maltese Parliament enacted the Electronic Communications (Regulation) Act, 2004 (hereinafter referred to "ECRA") and the Electronic Communications Networks and Services (General) Regulations, 2004 (hereinafter referred to as the "ECNSR'').

The fifth Directive on Privacy establishing users' rights with regard to the privacy of their communications was transposed on 10th January 2003 (Legal Notice 16 of 2003 under the Data Protection Act).

[1] Transposed into Maltese legislation on 14th September 2004.

The Directives oblige national regulatory authorities ("NRAs") such as the MCA to carry out reviews of competition in electronic communications markets to ensure appropriate and proportionate regulation in the light of ongoing changes in market conditions.

Each market review is subdivided into three phases:

- The definition of the relevant market or markets;
- An assessment of competition in each market(s); and
- An assessment of whether and what type of regulatory intervention is necessary.

More details and guidance concerning the conduct of market reviews are found in the Directives, the ECRA, and the ECNSR, together with other documents issued by the European Commission and the MCA.

1.1 Market Review Methodology

The EU Recommendation on relevant product and service markets within the electronic communications sector provides a common approach for NRAs in the identification of those telecoms markets for which regulatory intervention is warranted. The Recommendation originally came into force in July 2003 (Rec. 2003/311/EC). After having been in force for more than four years, the Recommendation came up for review and was eventually revised. The revised Recommendation[2] was then published in December 2007.

This process brought about some very important developments. Of significant relevance was the proposal to reduce, from 18 to 7[3], the number of markets for which the EU Commission recommends regulatory intervention.

Beyond these markets regulators could still intervene. However, NRAs would need to present the case with the EU Commission to justify their intervention in markets that have been excluded from the Recommendation.

At the same time, the principles behind the framework and the ground rules for how telecommunications are regulated across the EU have not changed. The revised Recommendation remains set to promote further harmonisation across the European Community by ensuring that the same product and service markets are subject to a market analysis in all Member States.

From a national view point, the MCA's document entitled 'Market Review Methodology' elaborates on the criteria used in assessing competition in Maltese electronic communications markets[4]. In this respect, the Recommendation, the EU Commission guidelines on market analysis ("Market Analysis Guidelines"), and the guidelines on the

[2] On 17 December 2007, the European Commission adopted the 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 and services. This replaces the earlier 2003 European Commission Recommendation.

[3] The revised Recommendation takes the view that the wholesale call termination on public telephone networks provided at a fixed location should remain susceptible to ex-ante regulation.

[4] Link to MCA market review methodology: http://www.mca.org.mt/infocentre/openarticle.asp?id=513&pref=1

assessment of SMP (the "SMP Guidelines") assume much relevance to the analysis of a product or service market under investigation (see Regulation 8 of the ECNSR).

Regulation 6 of the ECNSR stipulates that the results of market reviews carried out by the MCA and the proposed remedies shall be notified to the European Commission and to other NRAs. If the Commission is of the opinion that the market definition or proposals of whether to designate or not an operator with SMP would create a barrier to the single market, or if the Commission has serious doubts as to its compatibility with Community law and issues a notice under Article 7(4) of the Framework Directive, the MCA is required by Regulation 6 of the ECNSR to delay adoption of the proposed measures for a further period of 2 months while the Commission considers its position.

The market reviews are also supported by market data, which is collected from various internal and external sources, including users and providers of electronic communications networks and services and from regular consumer surveys.

1.2 National consultation and notification to the EU Commission

As required by Article 10 of the ECRA, the MCA published the results of this market review for national consultation, which ran from the 14th of December 2009 to the 15th of February 2010. This exercise elicited one response from Vodafone (Malta) Ltd.

In accordance with Regulation 6 of the ECNSR, the MCA subsequently notified the EU Commission with the outcome of the national consultation process, and its proposed approach to regulatory intervention.

EU Commission comments underlined the need for cost-oriented price caps, glide paths, or interconnection rates determined in any other way to be notified under Article 7(3) in conjunction with Recital 15 of the Framework Directive.

1.3 Liaison with Competition Authority

The MCA notes that, in accordance with Regulation 10 of the ECNSR, this market review has been undertaken on agreement with the National Competition Authority ("NCA").

This is also in line with the cooperation agreement signed on the 20th May 2005 between the MCA and the Office of Fair Competition ("OFC")[5]. The official position of the OFC is found in the Appendix to this document.

1.4 Scope of this Review

This review considers wholesale call termination on individual public telephone networks at a fixed location in Malta (hereafter also referred to as the "wholesale call termination").

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[5] Link to Memorandum of Understanding between MCA and OFC: http://www.mca.org.mt/infocentre/openarticle.asp?id=656&pref=9

1.5 Structure of the Document

The document comprises three more chapters as follows:

Chapter 02 outlines the market definition process, highlighting evidence (or the lack of it) for demand side substitution, supply side substitution, and potential competition.

Chapter 03 presents an analysis of dominance in the market, considering a number of criteria for the assessment of SMP.

Chapter 04 outlines the nature of the competition problems identified, and lists obligations on operators designated with SMP.

Chapter 2 - Market Definition

2.0 Outline

This chapter defines the market(s) for wholesale call termination on individual public telephone networks at a fixed location.

Markets are defined on the basis of a combination of a product/service and geographic dimension. In this regard, the MCA first defines the product markets by determining which products/services fall within the scope of this market review. It then determines the geographic area of the identified market(s).

This market definition exercise is forward looking in nature and, where it is deemed possible, those market conditions that may change significantly during the timeframe of this review are taken into consideration. It shall also serve as the basis on which to assess competitive constraints on the price-setting behaviour of service provider(s) active in the identified market(s), details in Chapter 3.

2.1 The regulatory basis for defining markets

It is worth recalling that Regulation 10 of the ECNSR stipulates that an NRA tailors its market definition on national circumstances, taking utmost account of all applicable guidelines and the revised EU Recommendation issued by the European Commission.

There are various dimensions related to the market definition procedure. Paragraph 2.1 of the Commission's Recommendation on relevant markets states that *'As the market analysis carried out by the NRAs have to be forward-looking, markets are defined prospectively. Their definitions take account of expected or foreseeable technological or economic developments over a reasonable horizon linked to the timing of the next market review'*.

The MCA's forward-looking approach to market definition is set out according to the EU Commission's Recommendation and Guidelines. In accordance to Recital (7) of the Recommendation, this procedure starts from a characterisation of the retail market over a given time horizon, taking into account the possibilities for demand-side and supply-side substitution.

Paragraph 4 of the above-mentioned Recommendation adds that markets shall be examined in a way which is independent of the infrastructure being used, as well as in accordance with the principles of Competition Law. Taking this into account, the MCA's approach to market analysis is based on a Competition Law assessment of markets and an assessment of the extent to which switching among products and services by consumers constrains prices, irrespective of the infrastructure deployed by the supplier.

2.2 Local operators in the fixed line sector

The fixed line telephony sector is characterised by five public telephone networks, which are currently providing wholesale call termination at a fixed location, namely:

- GO plc currently operates an IP fixed telephony network based on an NGN setup. Since NGNs rely on packet-based rather than circuit-switched solutions, NGNs are more streamlined in the way they convey calls. GO is able to cover the national territory with four fully-meshed media gateways as opposed to the fifteen PSTN switches previously in operation.

At a retail level, GO provides fixed line and mobile telephony services, broadband and Internet services, including voice over Internet protocol ("VoIP") services, and broadcasting digital Pay TV services. It also offers mobile telephony services via Mobisle Communications Ltd, its subsidiary more known as GO Mobile.

As at the end of Q3 2009, GO accounted for 77 percent of all local fixed line subscriptions, 31 percent of all Pay TV subscriptions, and for 43 percent of all mobile subscriptions and broadband Internet subscriptions.

GO plc was formerly known as Maltacom plc prior to November 2007. The companies' subsidiaries include Innovate Software Ltd, Mobisle Communications Ltd, Telepage Ltd, Multiplus Ltd, Worldwide Communications Ltd, and Innovate Ltd.

- Melita plc currently operates a hybrid fibre coaxial ("HFC") cable network, deployed in an NGN setup and with a ubiquitous coverage of Malta. Ten years ago, Melita started offering high speed Internet access across its HFC network via cable modem, and as from July 2005 it also introduced a packet/IP-based voice service. The company also offers IP-based digital Pay TV services. Last year Melita also launched its mobile voice and data services.

  As with GO, Melita is interconnected with all other local network operators.

  Figure 1 shows that Melita's share of total fixed line subscriptions as at the end of Q3 2009 stood at 23 percent, up from 20 percent in the corresponding period a year earlier. Melita's share of total broadband subscriptions as at the end of Q3 2009 stood at 50 percent, whilst its share of total PAY TV subscriptions stood at 69 percent.

  The company was formerly known as Melita Cable plc prior to September 2008. The companies' subsidiaries include Melita Infrastructure Ltd, Melita Mobile Ltd, and Melita Capital plc.

- Vodafone Malta Ltd currently offers mobile and broadband Internet services. Fixed line telephony services are offered over Vodafone's WiMAX network using the fixed broadband standard or D-standard, deployed in June 2008. These services are however only offered as an add-on to one of the retail broadband packages launched by the company. Vodafone's network is also based on an NGN setup and has a nationwide coverage.

  Figure 1 shows that, as at the end of Q3 2009, Vodafone's share of total fixed line subscriptions stood at 0.1 percent. A slightly higher market share of 3 percent for broadband has been recorded. Vodafone's share of total mobile subscriptions is however significant, standing at 50 percent as at the end of Q3 last year.

- SKY Telecom Ltd currently offers IP telephony and broadband Internet services over its own separate broadband wireless access ("BWA") network called SKYNet. SKYNet is a completely independent Broadband Wireless Access network, deployed in 2008 using a proprietary Motorola standard – PTP600. This standard provides an air interface which is totally independent of WiMAX BWA and operates in the 5.4Ghz 'unlicensed' band.

The coverage of SKYNet currently accounts for approximately 65 percent of the population using 6 x 360° Access Points and 1x60°x6 Access Point arranged in a star configuration for resiliency. Telephony services provided over SKY's air interface comply with all PATS obligations in terms of interconnection, 112, location and CLI, and portability amongst others. SKYNet voice and broadband services were launched on the market in February 2009.

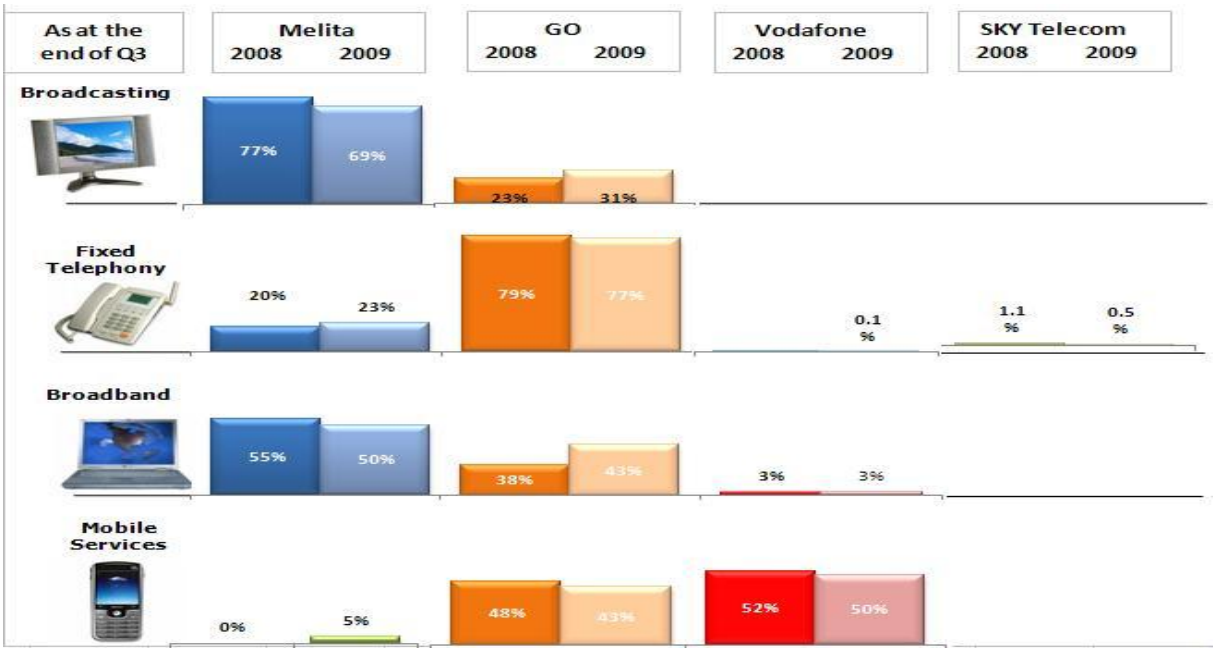
As at the end of Q3 2009, SKY Telecom's share of total fixed line subscriptions stood at 0.5 percent.

- Solutions and Infrastructure Services Ltd (also known as SIS Ltd), currently offers IP-based telephony and Internet services via its Network Operating Centre at Tigne` Point, Malta.

  This operator provides self-supplied wholesale call origination for the purposes of providing retail call services to its clients within a private area. SIS has two interconnection agreements, one with GO and another with Vodafone. SIS's infrastructure occupies a small geographic footprint and services a very small number of end-users. It has its own network switch, and can therefore terminate calls over its own network.

  The company is a joint venture between local developer Midi plc and technological partners Siemens S.p.A.

Figure 1



2.3 The boundaries underlining call origination, termination, & transit

In its latest assessment of the markets for wholesale call origination services, and wholesale transit services, the MCA underlined that:

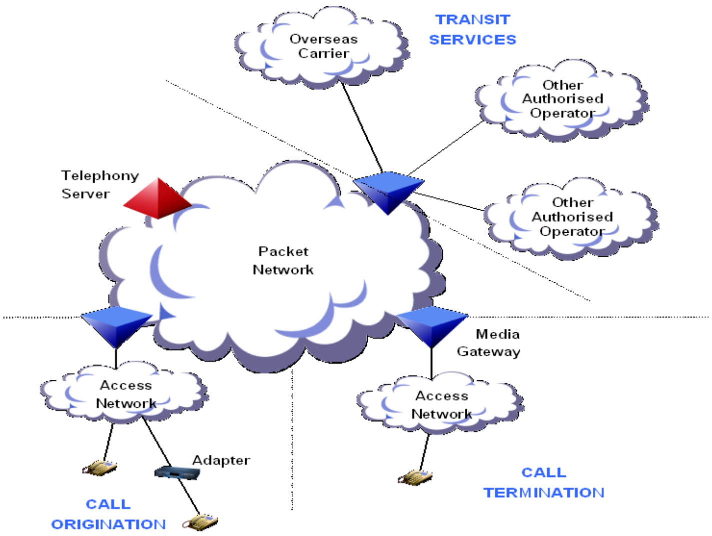
- *Wholesale call origination services* comprise call set-up, switching, and connection for the initial stage of the call. They incorporate conveyance from an end-user to the next stage in the call routing (either call termination or to the point of interconnection); and

- *Wholesale transit services* comprise the conveyance of traffic through, at least, one media gateway. By this definition, wholesale national transit services comprise the conveyance of traffic through one or more media gateways on the same network (namely the conveyance of on-net traffic), and the conveyance of traffic between media gateways of different operators (namely the conveyance of off-net traffic, depending on the type of call), which also includes the 'pure' conveyance of traffic across a third party transit operator. Wholesale transit services also encompass the conveyance of traffic through international switching centres.

The MCA is now reviewing its 2006 Decision regarding wholesale call termination services provided at a fixed location in Malta[6]. The 2006 Decision defined *wholesale call termination* services as comprising call completion and switching functionality at the terminating end of a call i.e. the conveyance of calls from the end of the previous stage (either call origination or to the point of interconnection), to the called end-user via the local-loop.

The NGN market boundaries highlighted above are depicted in Figure 2.

Figure 2



2.4 The retail level

The first part of the market definition exercise considers whether competitive constraints at the retail level could sufficiently influence the price-setting behaviour of service providers when setting the rates for wholesale fixed line call termination.

2.4.1 Demand-side analysis at the retail level

In a perfectly competitive environment, an increase in the price of a product or service should entice customers to switch to alternatives, thereby constraining prices back to their 'original' level.

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[6] Link to MCA Decision regarding 'Wholesale call origination, call termination and transit services provided over fixed electronic communications networks': http://www.mca.org.mt/infocentre/openarticle.asp?id=880&pref=1

The MCA considers whether this rationale is applicable in the case of fixed line call termination, given that the provision of this service is governed by the Calling Party Pays ("CPP") principle.

This principle underlines that the calling party pays for the whole cost of the call - including termination charges - whilst the recipient of the call (hereafter also referred to as the 'called-party') incurs no charge for answering an incoming call.

The first step in this analysis assesses the existence of any demand-side substitution at the retail level for fixed line call termination.

A End-user behaviour - awareness and sensitivity to call termination charges

As any telephone number is unique to a particular subscriber's fixed location, the calling party will generally know to where and to whom the call is being made, even though, there are instances when the network provider to which the number of the called party is assigned may not be known[7]. Nonetheless, any call to a specific number will result in the call being delivered to the network with which the dialled or called number is associated.

As already highlighted above, there are costs associated with terminating a call on a public telephone network, which are incurred by the originating operator and subsequently passed on to the calling party in the retail price paid for a call.

At a retail level, pressure on wholesale call termination rates could arise from customers that are aware of call termination charges, so much so that it determines their choice of network to make or receive the said call.

In theory, therefore, if a fixed line operator A increases the charges for terminating calls on its network, a calling party subscribed with fixed line operator B would have to face higher termination costs when making an off-net call to a number assigned with operator A. In response to the termination price changes at the retail level, the calling party would have an incentive to switch to constraining substitutes, such as by considering changing networks[8].

However, the MCA underlines that most end-users are not even aware of the tariff they pay for an on-net or off-net call[9], thereby suggesting minimal awareness of the call termination charge element.

Fixed line operators are also currently offering various calling plans bundling a varying number of 'free' on-net and off-net fixed-to-fixed ("FTF") minutes in the monthly rental charge[10]. In this regard, the lack of distinction between making an on-net or an off-net

[7] The availability of number portability allows end-users to keep the same number even when changing their service provider. In these circumstances, it is more difficult for the calling party to identify the network to which the called party is subscribed and the termination charges that apply.

[8] This may not be necessary if the calling party has multiple fixed line subscriptions at his/her residence, i.e. a subscription with both operators A and B. This makes it possible for the calling party to make an 'on-net' call and thereby avoid call termination charges. The MCA however notes that only a small share of end-users have multiple fixed line subscriptions. According to the MCA's Consumer Perceptions Survey on fixed line telephony carried out in June 2009, only 7.7 percent of local end-users have multiple subscriptions at home. Furthermore, given the CPP principle, it is very unlikely that such users are connected to two or more networks concurrently for the purpose of terminating calls.

[9] According to the MCA's Consumer Perceptions Survey on fixed line telephony, over 60 percent of respondents claim that they do not know how much an on-net fixed-to-fixed call costs. 79 percent of the respondents also claim that they do not know how much an off-net FTF call costs.

[10] The applicable rates for FTF calls beyond the 'free' minute allotment would then vary according to the choice of the calling plan (a higher number of 'free' minutes entails more 'expensive' monthly plans).

FTF call blurs the notion of termination charge differentials between terminating operators. This means that, even when subscribers are aware of the identity of the terminating operator, the significance of having such knowledge is not sufficient to constrain the pricing behaviour of termination providers.

The availability of number portability and flat-rate plans minimise the relevance of substituting from an off-net to on-net FTF call for the purpose of avoiding call termination charges. All in all, switching between operators or substitution between off-net and on-net calls on the basis of the call termination charge is not practical[11]. This implies that the calling party cannot exercise sufficient downward pressure on a price increase in call termination.

The MCA also considers whether there is a case for the called party to exercise pressure on a price increase in call termination. The MCA reiterates that wholesale call termination on individual public telephone networks is governed by the CPP principle, underlining that it is the calling party who pays for the retail cost of the said call, including a price increase in call termination.

On the other hand, the recipient of the call – the called party - incurs no charge for answering an incoming call. In this scenario, called parties remain indifferent to call termination charges imposed by their network operators, and are therefore not concerned in exercising pressure on such charges.

The above suggests that FNOs have no incentive to maintain low termination rates given that their subscribers are not price sensitive to call termination charges. The called party would not care about the termination charges incurred by the calling party in the retail price it pays for a call[12]. In reality, it would care most about the subscription fees and retail call rates that would apply once subscribed to a particular service provider, rather than what others had to pay in order for his/her assigned number to be reached[13].

B End-user behaviour - the use of mobile

The MCA also considers whether a price increase in fixed line call termination could, in theory, encourage substitution from FTF calls to mobile-to-fixed ("MTF") calls. It also considers whether mobile-to-mobile ("MTM") calls could substitute MTF calls and FTF calls, so much as to sufficiently constrain a price increase in fixed call termination.

In its Decision entitled 'Retail public telephone call services provided at a fixed location' published in March 2009 the MCA underlines that not all fixed line telephone subscribers may own a mobile subscription and that, vice versa, not all mobile subscribers may have a fixed line subscription. This Decision also underlines that a significant price differential exists between mobile-originated calls, and fixed line-originated calls.

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[11] The MCA also notes that local bundle packages including fixed line telephony as one of the bundled services, only allow for the take-up of calling plans which are offered against a monthly rental charge when taken on a stand-alone basis. With an ever increasing take-up of such bundle packages, the possibility for a calling party to consider substituting off-net fixed-to-fixed calls with their on-net counterpart dissipates further.

[12] Indeed, the end-users would only see a global retail tariff encompassing the wholesale call termination rate and other cost components. Consequently, the end-user cannot detect any changes in termination charges and cannot exert pressure on the setting of wholesale call termination rates.

[13] This may suggest that call termination is part of a cluster of fixed line services. However, given the lack of customer awareness regarding call termination charges, voice call termination is actually purchased on an individual basis at the wholesale level. This means that the provision of voice call termination should be considered separately to other fixed line services.

The Decision determines that a FTM call is generally more expensive to the calling party than a FTF call. This suggests that, even if the called party is not reachable via the latter type of call, the calling party would not undertake a FTM call unless required to do so for immediate communication. In addition, substitution to a FTM call is limited given that not all fixed line users have a mobile subscription. On the other hand, a MTF call leaves the calling party in the same position as that noted for a FTF call, given that the cost of terminating a call on a fixed line network generally does not vary with the network originating the call.

The called party would also be indifferent to a price increase in fixed call termination by the network operator hosting his/her fixed line number. As argued in previous sections, fixed line call termination is governed by the CPP principle. This means that the called party is relatively insensitive to the pricing and costs of termination on public fixed telephone networks. In this sense, the behaviour of the called party is not expected to limit a provider's ability to charge others high(er) prices for call termination. Only if the called party cared about what others have to pay in order for him/her to be reached, that a small but significant non-transitory increase in the price for call termination would induce the called party to arrange and have calls terminated via other forms of communication and/or via another network. Overall, end-users lack awareness of call termination charges, thereby suggesting that called parties are insensitive to changes in termination fees charged by operators hosting the assigned number.

Regarding MTM calls as a substitute to MTF calls and FTF calls, the MCA notes again the significant price differentials observed for these different types of calls. These price differentials are partly attributed to the higher termination charges for calls terminated on mobile networks. The MCA therefore argues that MTM calls are unlikely to constrain fixed termination rates to a competitive level.

C End-user behaviour - the use of managed voice over broadband ("VoB") services

Managed VoB services are currently being offered by Vodafone, which is currently offering an IP-based telephone service to its customers through its WiMAX network. This offer is only valid if the customer purchases a broadband connection with the same operator.

The MCA notes that, in terms of functionality, a VoB call offered by Vodafone, could be substitutable with a conventional call offered by all the other FNOs. However, in the event of a hypothetical monopolist increasing the price of terminating a fixed line call, it is very unlikely that customers switch to VoB services in response to price movements at the retail level.

This is because, firstly, most customers are not aware of the applicable termination charges, and, therefore, are insensitive to the pricing and costs of terminating a call on a public telephone network. It is therefore very unlikely that switching to VoB materialises in the event of a price increase in call termination.

Secondly, in the case of Vodafone's VoB offers, customers must first invest in a broadband internet connection before switching to Vodafone's VoB services. In this regard, the revised EU Recommendation states that, generally, consumers will not upgrade to a broadband service solely for the purpose of accessing voice services.

The MCA is also of the opinion that users purchasing fixed access via a wireless broadband connection primarily do so to get access to higher-speed internet services and not essentially to avail of VoB services.

Consequently, the MCA considers that a small but significant price increase in FTRs would not be constrained by an end-user(s) switching to VoB.

D End-user behaviour - the use of unmanaged voice over broadband (VoB) services

End-users could install a particular type of software on their computer, which enables the delivery VoB services, which are not managed by an intermediary or service provider. These unmanaged VoB services, are classified according to:

- those that only enable users to make calls to other PC users over the Internet; and

- those that enable users to make calls to any E.164 number from their PC. In this case, the user enters into a commercial agreement with a local VOIP service provider, which could possibly be other than the user's broadband access provider or ISP.

Regarding these type of VoB services, the revised EU Recommendation states that "*on the basis of quality differences and product characteristics, unmanaged VoB services appear for the time being to be less of a substitute for narrowband telephony than managed VoB, but that distinction may disappear over time as the quality of unmanaged VoB services improves and technical features change*".

The MCA believes that, within the timeframe of this review, unmanaged VoB services will not sufficiently constrain a small but significant price increase in FTRs associated with the termination of conventional IP-based calls.

2.4.2 Supply-side analysis at the retail level

The MCA underlines that, even in the event of a 5 to 10 per cent increase in the wholesale call termination charge of a terminating operator, an originating operator cannot terminate a call to a number assigned with the said terminating operator on some other network. This scenario holds irrespective of whether the originating operator wants to terminate the call directly or else via an intermediary i.e. a third party transit provider. As a result, supply side substitution at the retail level is not expected to constrain call termination at the wholesale level.

Conclusion

The MCA considers that the calling party cannot bypass the terminating fixed line network hosting the called number. If the calling party tries to terminate a call on a network other than that to which the called number is assigned, this call would be unsuccessful.

The calling party has no influence whatsoever over the called party's choice of network, and therefore has to pay the respective termination charge(s).

The absence of demand-side and supply-side substitution for call termination at the retail level suggests that no effective competitive constraints can be exerted from the retail level to call termination at the wholesale level.

2.5 The wholesale level

The second part of the market definition exercise assesses the existence of any competitive constraints at the wholesale level which could influence the price-setting behaviour with respect to fixed line call termination.

In line to what has already been outlined in previous sections, the prevalence of the CPP principle does not incentivise operators to maintain low wholesale termination rates given that, in the event of a price increase for fixed line call termination, the originator of the call cannot bypass the network to which the called number is assigned. In particular, the originator of the call cannot bypass the terminating network, and each fixed line operator would still be the only supplier of call termination on its own network.

In this regard, the termination cost element of a call is actually borne by the originating operator, resulting in a direct payment flow towards the terminating operator. Such a payment flow would apply for the termination of directly connected calls, i.e. where termination services are acquired by an originating operator to terminate fixed calls directly. In the case of calls to end users via CPS operators, the payment flow is similar except that a payment has also to be made to the originating operator (the originating charge) in addition to the payment to the terminating operator.

2.5.1 Demand-side analysis at the wholesale level

Call termination on a number assigned with a public telephone network cannot be terminated elsewhere; otherwise the call would turn out unsuccessful.

The lack of demand-side substitution for wholesale fixed line call termination suggests that the purchaser of call termination cannot bring pressure to bear on its supplier (or terminating network) to prevent a price increase for the service it is buying.

This would ultimately translate in higher prices for call termination, with suppliers of call termination reaping larger revenues.

2.5.2 Supply-side analysis at the wholesale level

From a supply-side perspective, the MCA takes into account the effectiveness and immediacy of a supplier's response to a price increase in wholesale call termination.

Given the lack of alternatives for conveying and terminating a call on a number other than the network operator to which it is assigned, the MCA considers that it is highly unlikely for originating operators to curb market power over termination enjoyed by FNOs.

In the event of a hypothetical 5 to 10 percent increase in the price for call termination, alternative network operators ("OAOs") would not be able to provide termination services on the network of the hypothetical monopolist. Instead, OAOs would probably increase their own price of call termination to match the rates charged by the hypothetical monopolist.

Conclusion

Given the present level of technology, there is no possibility of any demand-side or supply-side substitution for wholesale call termination over a terminating network operator. Termination on each individual network therefore constitutes a separate relevant market.

2.6 Geographic market

According to EU Commission guidelines, a relevant geographic market 'comprises an area in which the undertakings concerned are involved in the supply and demand of the relevant products and services in which area the conditions of competition are similar or sufficiently homogeneous and which can be distinguished from neighbouring areas in which the prevailing conditions of competition are appreciably different'. The Commission's SMP Guidelines also refer to the use of two criteria in determining the geographical scope of a relevant market, namely the area covered by a network, and the existence of legal and other regulatory instruments.

On the basis of the above-mentioned guidelines, the MCA found sufficient evidence to justify a national market definition for the provision of wholesale call termination on individual public telephone networks at a fixed location. Each individual fixed network operator is considered to represent a separate relevant market for the provision of wholesale call termination services. The geographic scope of each market reflects the extent of physical coverage that characterises the respective network operator.

Conclusion

Given that each FNO is licensed on a national basis and offers geographically uniform FTRs, the MCA concludes that each market identified in this review shall be considered as a national market.

DECISION 1

The identification of markets

In respect of the market definition exercise, and in accordance with competition law principles, the MCA has identified five relevant markets for wholesale call termination services in Malta, namely:

- Wholesale fixed call termination provided by GO plc;
- Wholesale fixed call termination provided by Melita plc;
- Wholesale fixed call termination provided by SKY Telecom's SKYNet;
- Wholesale fixed call termination provided by Vodafone (Malta) Ltd; and
- Wholesale fixed call termination provided by SIS Ltd.

Each relevant market includes call termination services provided by each FNO to third party operators (irrespective of the technological platform), and also self-supplied termination.

Chapter 3 - Market Analysis

3.0 Outline

Chapter 3 presents an analysis of dominance in the identified markets. In this analysis the MCA considers a number of criteria for the assessment of significant market power ("SMP"), namely market shares, barriers to entry and potential competition, and countervailing buyer power ("CBP").

3.1 Background to Market Analysis

According to the ECRA, SMP is defined as follows:

"A position equivalent to dominance enjoyed by an undertaking either individually or jointly with others that is to say a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers."

Article 8(4) of the ECRA introduces the concept of leveraging of market power and states that:

"Where an undertaking has significant market power on a specific market, it may also be deemed to have significant market power on a closely related market, where the links between the two markets are such as to allow the market power held in one market to be leveraged into the other market, thereby strengthening the market power of the undertaking".

In its assessment of SMP, the MCA takes utmost account of the Commission's SMP Guidelines as well as the MCA's equivalent guidelines.

3.2 Assessment of SMP

The MCA is hereby providing an analysis of the conditions prevailing in the identified markets. The approach implemented by the MCA ensures that the analysis captures the dynamic factors that shape the said markets.

3.1.1 Market shares

The MCA notes that high market shares are not in themselves decisive as to whether an undertaking enjoys SMP in a market. Nonetheless, market shares that exceed the 50 per cent threshold would generally raise the presumption of SMP. This is in line with EU Commission Guidelines which underline that, according to established case-law, market shares in excess of 50 percent are in themselves, save in exceptional circumstances, evidence of the existence of a dominant position.

The area covered by each FNO is considered to constitute a separate wholesale termination market given that termination on a particular network operator cannot be substituted by termination on any other network. This implies that each FNO has a 100 percent market share in the termination of calls over its own network.

Each FNO has an implicit 100 percent market share both in terms of the volume of minutes terminated over its own network and in terms of the revenues generated respectively.

In the absence of regulation, FNOs would have all the pricing freedom derived from their monopoly power over termination. FNOs would therefore be able to set wholesale termination charges above the competitive level, in order to maximise revenues.

Conclusion

The MCA considers each FNO to have a 100 percent market share in the provision of termination services over its own network, irrespective of its size and technological platform.

3.1.2 Entry deterrence and potential competition

FNOs could exercise market power by foreclosing markets, and by engaging in tactics that deter market entry.

In considering fixed line call termination, the MCA argued that each FNO has a 100 percent market share on call termination over its own network, and that there are no constraining substitutes to this market 'outcome'. This means that FNOs are not in any way threatened by potential competition in their supply of call termination.

The implication of the above is that FNOs enjoy an inherent dominant position on call termination over their own network, with no possibility for supply side substitution.

Wholesale call termination is also governed by the CPP arrangement, suggesting that it is not possible to terminate a fixed line call other than on the network to which the called party is subscribed. In the absence of regulatory intervention, an FNO could possibly exploit this measure of market power by increasing the price of termination above the competitive level. Ultimately, such increases could feed-through in higher retail call rates for consumers.

Given the current level of technological developments, this market condition is set to prevail within the timeframe of this market review.

Conclusion

FNOs have the ability to exercise market power by setting termination rates above the competitive level. In this regard, no operator can deprive FNOs from their pricing freedom derived from their monopoly power over termination as the provision of wholesale call termination over another network is not replicable. This implies that each service provider's network characterising the identified markets face no threat of potential competition.

3.1.3 Countervailing buyer power ("CPB")

This assessment of CBP takes into account two main considerations. Firstly, it considers the relative strength of CBP at the retail level in influencing the price of call termination, i.e. CBP of subscribers connected to networks (hereafter also referred to as 'customers'). Secondly, it considers the relative strength of CBP at a wholesale level in the setting of prices charged for call termination, i.e. CBP of FNOs and MNOs providing telecommunication services to the said subscribers.

Customers with a strong negotiating position could exercise a significant impact on the behaviour of operators and thereby influence market outcomes. The stronger the CBP of customers, the more service providers are restricted from exercising market power, and the less they are able to act independently of their customers.

In this regard, CBP exists if customers have a sufficiently strong 'negotiating' position to influence and effectively prevent an attempt by the supplier to increase prices above the competitive level. The extent of customer CBP depends on whether customers are able to bring some pressure to bear on the supplier by resorting to constraining substitutes, for example by not purchasing the service or product from that particular supplier and possibly switch to alternatives.

However, customers are not able to sufficiently influence the price charged for call termination as, under the CPP principle, a called party does not sufficiently care about the costs that the calling party incurs to terminate the call. Furthermore, the calling party does not have a choice as to where to terminate the call since it is the called party that chooses the network hosting the number to be reached. Based on this reasoning, customers have no CBP to prevent a price rise for call termination.

Another consideration in the assessment of CPB relates to market dynamics at the wholesale level. The following sections consider whether a service provider purchasing call termination could be sufficiently important to its supplier to influence the price charged for the service. For this purpose, the MCA considers the share of fixed termination minutes purchased by local FNOs or MNOs.

Table 1

Traffic terminated on public telephone networks provided at a fixed location	2008		2009	
	Q3	Q4	Q1	Q2
Fixed-to-fixed traffic	134,003,659	144,815,617	154,016,750	153,542,772
On-net minutes	107,570,637	116,011,230	123,931,843	121,403,228
Off-net minutes	26,433,022	28,804,387	30,084,907	32,139,544
Mobile-to-fixed traffic	5,760,614	5,808,647	6,166,890	7,260,818
Traffic originated from foreign network operators	5,660,077	5,535,310	5,510,654	5,283,413

Table 2

Percentage of traffic terminated on public telephone networks provided at a fixed location	2008		2009	
	Q3	Q4	Q1	Q2
Fixed-to-fixed traffic	92.15%	92.74%	92.95%	92.45%
On-net minutes	73.97%	74.29%	74.80%	73.10%
Off-net minutes	18.18%	18.45%	18.16%	19.35%
Mobile-to-fixed traffic	3.96%	3.72%	3.72%	4.37%
Traffic originated from foreign network operators	3.89%	3.54%	3.33%	3.18%

Table 1 and Table 2 show that MNOs only 'buy' a small share of call termination minutes supplied by local FNOs. This means that the relative bargaining strength of mobile operators in respect of their traffic terminating on FNOs is not sufficient to credibly threaten the monopoly power enjoyed by fixed operators over termination. This implies that MNOs do not have sufficient CBP to influence the price charged for fixed call termination by their suppliers.

The MCA is also of the view that the obligation on MNOs to interconnect also deprives MNOs from any CBP they might have in the setting of MTF termination rates. In this regard, even if the obligation to interconnect is not mandated and MNOs did have buyer power, a threat from MNOs not to purchase call termination by cutting-off interconnection with any of their fixed counterparts would carry limited significance, especially with the larger network operators.

If the threat not to interconnect was actually implemented by any MNO, more harm would be inflicted on its own subscribers rather then on the network to which interconnection has been cut-off. Those MNOs trying to exercise CBP in this way would damage their own reputation as their own customers would not be able to make calls to all local networks, thereby ending up getting 'less value' from their subscription. This approach would dent their negotiating position even further.

Local MNOs cannot therefore pose a credible threat not to purchase termination from a local FNO. This leaves local FNOs free to set MTF terminating charges to a level above the competitive outcome.

The MCA will now assess the relative bargaining strength enjoyed by incumbent FNOs and OAOs in determining the setting of FTRs. Based on the analytical approach outlined in the previous sections, the MCA examines the sufficiency of CBP of these network operators by referring to the traffic terminating on each.

Minutes terminated on fixed line networks include the termination of minutes originated and terminated within the same fixed network (self-supplied minutes) and the termination of (off-net) minutes originated from one network and terminated on a different one (i.e. when FNOs purchase termination services from each other).

On considering self-supplied call minutes, Table 3 shows that GO registered substantially strong levels of on-net traffic in the period under consideration. In this respect, GO accounted for 82.7 percent of all self-supplied call minutes registered by all operators for Q2 2009.

Table 3

Traffic terminated on public telephone networks provided at a fixed location	2008		2009	
	Q3	Q4	Q1	Q2
On-net fixed-to-fixed (self-supplied) call minutes	107,570,637	116,011,230	123,931,843	121,403,228
terminated on GO	89,146,631	94,938,365	101,022,382	100,344,201
terminated on Melita	18,423,636	21,071,827	22,897,173	21,040,836
terminated on SKY Telecom's SKYNet	-	-	5,150	14,110
terminated on Vodafone (Malta)	370	1,038	2,117	1,192
terminated on SIS	-	-	5,021	2,889
Off-net fixed-to-fixed call minutes	26,433,022	28,804,387	30,084,907	32,139,544
terminated on GO	16,546,487	18,109,422	18,059,491	20,294,337
terminated on Melita	9,851,535	10,657,465	11,952,292	11,750,774
terminated on SKY Telecom's SKYNet	-	-	-	-
terminated on Vodafone (Malta)	35,000	37,500	51,433	73,909
terminated on SIS	-	-	21,691	20,524

On considering off-net call minutes terminated on each network operator, Table 3 also shows that, for Q2 2009[14], off-net call minutes terminated on GO accounted for 63.1 percent of the total for all operators. This result places GO as the biggest seller of call termination services to other local FNOs.

In terms of market share, GO is then followed by Melita, Vodafone (Malta) and finally SIS[15]. The MCA considers this finding as indicative of the relative bargaining strength of each network operator and the respective CBP that each could exert to mitigate the market power enjoyed by the terminating operator. In other words, the lower the placing in the aforementioned list, the less significant is the respective bargaining strength.

The MCA believes that, even in the absence of regulation, it is very unlikely that any OAO manages to exert sufficient CBP on the price charged for call termination on other networks. This is because OAOs are obliged to complete all calls whatever the terminating network. Therefore, any OAO would be in a similar position to that

[14] As at the end of this period GO accounted for 76.95 percent of total fixed line subscriptions in Malta, Melita accounted for 22.40 percent, Vodafone (Malta) accounted for 0.18 percent, SKY Telecom accounted for 0.45 percent, and SIS accounted for 0.04 percent.

[15] The corresponding figures for SKY Telecom's SKYNet were not readily available at the time of publication. Given the relatively recent deployment of SKYNet, the MCA has indications that, for Q2 2009, the number of minutes terminated on this network reached 230,000.

encountered by a MNO in that it cannot cut-off interconnection to constrain the price charged for call termination by other FNOs.

Table 4

Traffic terminated on...	Q1 2009		Q2 2009	
	Total	%	Total	%
Vodafone (Malta)	51,433		73,909	
originating from GO	37,172	72.27	71,830	97.19
originating from Melita	14,240	27.69	-	-
originating from other operators	21	0.04	2,079	2.81
SIS	21,691		20,524	
originating from GO	21,691	100.00	20,503	99.90
originating from Melita	-	-	-	-
originating from other operators	-	-	21.00	0.10

It is also evident from Table 4 that the main originators of traffic terminating on networks owned by Vodafone (Malta), SIS, and the newer SKY Telecom's SKYNet are GO and Melita. It is clear from the outset that, even in the absence of regulation regarding interconnection, OAOs would have no incentive in cutting-off interconnection with these two operators.

In circumstances where OAOs clearly lack buyer power, there is no other option other than to purchase call termination from GO and Melita, irrespective of the price charged for the service. In practice, OAOs cannot credibly threaten not to purchase termination from these operators, and thereby cannot exert CBP on the price being charged. This leaves GO and Melita free to set termination charges above the competitive level, absent regulation.

A similar reasoning can be deployed when taking into consideration the CBP of either GO and Melita. Again, assuming an unregulated environment, OAOs also enjoy that pricing freedom in setting FTRs, which is derived from their monopoly power held over termination. Indeed, a major selling point of incumbent and larger operators is that of ensuring seamless communication services for their customers, as is the case with OAOs. Overall, operators have no tangible commercial incentive to damage their reputation. Furthermore, in practice all FNOs are obliged to provide interconnection to all other operators.

In this regard, the MCA notes that it has mandated FTRs which have followed a downward trajectory towards the competitive level since 2004 as shown in Table 5 below.

Table 5

Interconnection Rates - Call Termination **(€ cents per minute excl. VAT or any other applicable tax)**	Day	Evening	Weekend	Average
Applicable as from 1st July 2003	0.055	0.016	0.028	-
Applicable as from 1st October 2004	0.028	0.008	0.014	0.018
Interconnection Rates - Call Termination **(€ cents per minute excl. VAT or any other applicable tax)**	Peak	Off-peak	Night	Average
Applicable as from 1st January 2006	0.019	0.013	0.005	0.012
Applicable as from 1st January 2007	0.012	0.009	0.003	0.008
Applicable as from 1st July 2008	0.012	0.008	0.003	0.007
Applicable as from 1st August 2009	0.008	0.007	0.005	0.007

Time periods indicated are as follows:

Day: from 6:00 to 18:00 on Monday to Friday including Public Holidays; Evening from 18:00 to 6:00 on Monday to Friday including Public Holidays; Weekend: from 00:00 to 24:00 on Saturday and Sunday

Peak: from 08:00 to 18:00 from Monday to Friday including public holidays; Off-peak: from 06:00 to 08:00 from Monday to Friday including public holidays from 06:00 to 18:00 on Saturdays and Sundays; Night: from 18:00 to 06:00 all week including public holidays

These rates were mandated because market forces are not sufficient to entice FNOs in bringing down FTRs to a competitive level on their own initiative.

Finally, the MCA has also considered that local FNOs terminate internationally originated calls on their own network. However, the share of international call minutes terminated on fixed line networks accounts for less than 4 percent of the total. The MCA is therefore of the view that foreign operators have no CBP in the setting of local FTRs.

Conclusion

The MCA finds no evidence that, within the timeframe of this review, and absent regulation, any wholesale operator or group of operators would have sufficient CBP to constrain some other operator in charging FTRs at a level commensurate with the competitive outcome.

DECISION 2

The designation of dominant operators with SMP

The MCA designates GO, Melita, SKY Telecom (via its WiMAX network SKYNet), Vodafone Malta, and SIS as operators enjoying SMP in the provision of wholesale call termination over their own network.

The MCA underlines that this decision has been based on the following findings:

- each FNO holds a 100 per cent market share on termination over its own network, irrespective of its size and technological platform;
- each FNO can act independently in the provision of wholesale call termination over its own network, as no operator can actually replicate the provision of wholesale call termination services over another network;
- each network operator characterising the market identified in this review faces no threat of potential competition; and that
- no wholesale operator or group of operators have sufficient CBP to constrain some other operator in charging FTRs at a level commensurate with the competitive outcome.

Chapter 4 – Regulatory Implications

4.0 Background

In accordance with Regulation 10(4) of the ECNSR, where an operator is designated as having significant market power (SMP) on a relevant market, either individually or jointly with others, the MCA is obliged to impose on such operator appropriate regulatory obligations, referred to in sub regulation (2) of Regulation 10 of the ECNSR, or to maintain or amend such obligations where they already exist.

This section highlights on the actual and potential competition problems that exist in the wholesale call termination market, and sets out the MCA's regulatory approach to address these problems.

4.1 Existing obligations

In the previous review of wholesale call termination on individual public telephone networks at a fixed location carried out in 2006 the MCA concluded that GO (formerly known as Maltacom) and Melita (formerly known as Melita Cable) held an SMP position in the wholesale call termination over their respective network. As a result, the identified markets (2 in total) were considered susceptible to *ex ante* regulation.

In accordance with Article 9(3) of the ECRA and regulation 10(4) of the ECNSR the MCA then acted in pursuit of its statutory obligations to ensure adequate access, interconnection and interoperability of services and other measures listed in regulations 18 to 22 of the ECNSR (wholesale obligations).

The MCA argued that, in view of their ability to exert market power, it had to impose obligations on both GO and Melita:

- to meet reasonable requests for access to, and use of, such wholesale access products, features or additional facilities forming part of the market for wholesale call termination services;
- to ensure transparency in making public specified information, such as accounting information, technical specifications, network characteristics, terms and conditions for supply and use, as well as prices;
- to behave in a non-discriminatory manner in the provision of access and, or interconnection by applying equivalent terms, conditions and charges in equivalent circumstances to other undertakings providing equivalent services, and by providing services and information to others under the same terms and conditions, at the same price, and of the same quality as provided for their own services, or those of their subsidiaries or partners.

In order to counteract the incentive of the identified SMP operators to charge excessive termination rates and so as to further strengthen the obligations of non-discrimination and transparency, the MCA also considered it necessary to apply a price control obligation. In this regard the MCA obliged Melita to peg any of its rates for wholesale termination, at a maximum, to GO's termination prices.

The MCA reserved the right to impose cost orientation and, or accounting separation and, or cost accounting obligations on Melita, and the right to demand any information or data to avoid pricing practices that are disruptive to the market.

Correspondingly, the MCA imposed the obligations of cost orientation, cost accounting, and accounting separation on GO. The imposition of cost orientation allowed the MCA to ensure fair and efficient access to GO's network and services. Correspondingly, the cost accounting obligation worked in effectively promoting competition and curbing possible abuse of dominance by GO in the wholesale termination market. The cost accounting system also provided the MCA with detailed information regarding GO's service costs and ensured that fair, objective, and transparent methodologies are followed by GO in allocating costs to the regulated services.

Finally, the obligation of accounting separation was instrumental in ensuring that GO does not price-discriminate between its retail arm and its competitors when providing access and interconnection at a wholesale level. Indeed, this obligation allowed the MCA to gather evidence on the wholesale and internal transfer prices of products and services of the undertaking with SMP, and ensured that GO charged non-discriminatory prices, whilst safeguarding against possible market failures such as cross-subsidisation and the application of margin squeeze.

4.2 Factors distorting competition

As explained in the previous chapter, each network operator characterising the identified markets enjoys SMP in the provision of wholesale fixed line call termination. The designation of SMP therefore serves to signal that, absent regulation, these network operators could potentially abuse of their monopoly position over termination, either by charging excessive prices for terminating calls onto its network, and/or by discriminating in the provision of access and, or interconnection.

4.2.1 Excessive pricing

Absent regulation, FNOs have an incentive to exploit their market power by setting excessive rates for terminating calls over their own network. Apart from increasing incoming termination revenues, FNOs also have an interest in moving subscribers and traffic over their own network.

If left unconstrained by regulation, any SMP operator would therefore set excessive termination charges for calls that are originated from other networks. This would allow the SMP operator to generate enough funds to potentially cross-subsidise its retail tariffs, and discriminate in favour of on-net calls to safeguard or enhance its market standing. This would distort competition as it dilutes the viability for new undertakings to consider market entry, even in closely related markets.

4.2.2 Discriminatory behaviour

Absent regulation, an SMP operator may have an incentive to leverage market power via price and non-price discriminatory behaviour. For example, an SMP operator could charge itself or its subsidiary lower FTRs than the corresponding rates set for interconnecting with other fixed or mobile operators. This behaviour forecloses competition, as smaller and/or newer operators would find it more difficult to compete in the retail market with the SMP operator.

Abusive behaviour by SMP operators could also be reflected in non-price discriminatory actions, such as discriminatory use, or withholding of, information, delaying tactics and the application of undue requirements for interconnecting.

Potential competition problems could also arise if abusive behaviour by SMP operators results in newer market entrants or alternative network operators ("OAOs") finding it difficult to sign or even failing to negotiate interconnection agreements.

4.3 MCA's regulatory approach

The MCA is mandating a number of obligations on SMP operators to ensure that efficient termination rates prevail in the identified markets, and that customers reap the benefits of competition.

The MCA holds the view that its regulatory approach addresses the nature of the competition problems identified above, and believes that each remedial action is proportionate and justified in light of the objectives set out in Article 4 of the Electronic Communications (Regulation) Act.

The MCA notes that it is unlikely for any single remedy to achieve the aim of ensuring effective competition by itself; hence, the MCA felt the need for a suite of remedies that complement, support and reinforce each other, including:

4.3.1 Access obligation

The MCA has the function, under Regulation 15 of the ECNSR, to ensure that electronic communications services provide end-to-end connectivity through the appropriate granting of access to, or interconnection with, other networks, without prejudice to an SMP designation. It is therefore authorised to impose obligations on undertakings that control access to end-users in order to ensure end-to-end connectivity where this is not already the case.

This market review confirms that GO, Melita, Vodafone, Sky Telecom's SKYNet and SIS have SMP on the market for voice call termination on their individual public telephone network. Therefore the MCA is of the opinion that the access obligation shall be imposed on these operators, in accordance with Regulation 21 of the ECNSR.

This obligation is to ensure interoperability of network services, as SMP operators are obliged to interconnect appropriately to each other for the purpose of terminating voice calls.

All SMP operators identified in this review are therefore required to provide other networks/undertakings with services needed to ensure interoperability of end-to-end services to users.

All FNOs shall provide network access for the provision of voice call termination services to every public electronic communications network providers who make such a reasonable request (Regulation 21(2) of the ECNSR). FNOs shall therefore negotiate in good faith with undertakings making new requests for interconnection services.

Interconnection services shall be provided together with any services, facilities or arrangements which are necessary for the provision of such services. The said FNOs shall also ensure that all reasonable requests for interconnection services are expedited in a fair, reasonable, and timely manner as required under Regulation 21(3) of the ECNSR.

The reasonableness or otherwise of the request shall be evaluated on the basis of Regulation 21(4) of the ECNSR and the decision to provide interconnection or otherwise will be subject to scrutiny by the MCA in accordance with its powers at law where negotiations between two parties fail.

In the latter case, the MCA will be the final arbiter in deciding whether the request is truly reasonable or otherwise.

SMP operators cannot withdraw access to termination facilities without prior authorisation in writing by the MCA.

4.3.2 Non-discrimination obligation

Non-discrimination ensures that FNOs do not provide wholesale services on terms and conditions that discriminate in favour of a particular undertaking. More specifically, the imposition of this obligation is intended to avoid a situation whereby an SMP operator would have the ability to exploit its market power in order to discriminate between self-supplied termination services and those supplied to other fixed or mobile operators.

The obligation in question targets all forms of discrimination as set out in Regulation 19 of the ECNSR, namely price and non-price discriminatory behaviour. Non-price parameters refer to competition problems related to the withholding of information, delaying tactics, undue requirements, low or discriminatory quality, strategic design of products, and discriminatory use of information.

The MCA holds the view that the imposition of a non-discrimination obligation would enable GO, Melita, Vodafone (Malta), SKY Telecom, and SIS to apply equivalent terms, conditions and charges in equivalent circumstances to other undertakings providing equivalent services, and to provide services and information to other operators under the same terms and conditions, at the same price, and of the same quality as they provide for their own services, or those of their subsidiaries or partners.

The MCA also deems it important that information gained by operators as a result of their provision of call termination services is not used by downstream retail providers in any manner as to favour their own operations.

4.3.3 Transparency obligation

The imposition of the transparency obligation on FNOs is to ensure that the access and non-discrimination obligations are observed. The transparency obligation would require FNOs to deliver services of equivalent quality to all operators and that alternative operators have sufficient information and clear processes to which they would not otherwise have access.

Regulation 18 of the ECNSR authorises the MCA to impose the transparency obligation on undertakings holding SMP in relation to interconnection and, or access (including wholesale call termination), requiring such undertakings to publish information on termination rates and to give advance notice of proposed changes to such rates. The transparency obligation also requires the said undertakings to make public specified information such as accounting information, technical specifications, network characteristics, terms and conditions for supply and use, and prices.

The Authority is obliging each operator designated with SMP in this review to publish a reference interconnection offer (RIO). The RIO shall be sufficiently unbundled to ensure that undertakings are not required to pay for facilities which are not necessary for the services requested, giving a description of the relevant offerings broken down into components according to market needs, and the associated terms and conditions including service level agreements and prices as directed by the MCA.

All SMP operators should provide and publish appropriate manuals, order forms and processes for services necessary for interconnection.

The Authority retains the right to impose changes to reference offers to give effect to the obligations imposed under the Act, and also reserves the right to specify the precise information to be made available, the level of detail required, and the manner of publication.

With respect to the publication of the RIO, all operators are to notify the MCA within 30 days from the publication of the decision with a draft RIO. Following the approval of the MCA, all SMP operators are to publish the approved RIO.

The MCA also reiterates that the RIO of all operators is to be made available on their respective websites and should be accessible to anyone without the need to get any prior registration and/or authorization from the said operators. Furthermore, the said operators shall notify the MCA with the exact location (link) on the Internet page where the RIO is published on their respective websites as soon as this is published.

The MCA is of the opinion that the transparency obligation instils confidence in the market that services are not provided on a discriminatory basis. It also helps avoid any possible disputes and accelerates negotiations between existing and potential operators.

The MCA maintains the right to establish or alter the extent of the obligation to publish information in the reference offer at a later stage.

4.3.4 Price control, cost accounting, and accounting separation

In order to counteract the incentive of SMP operators to charge excessive termination rates and so as to further strengthen the obligations of non-discrimination and transparency, the MCA considers it is necessary to apply a price control remedy[16].

In determining the level of regulatory intervention to ensure efficient FTRs, the MCA believes that it would be appropriate to take into account the requirement for proportionality, and the SMP position of each operator in the identified markets whereby none of the operators has an incentive to lower termination charges through self initiative.

The MCA reiterates that it stands by its rationale of implementing regulatory remedies to address potential competition problems in the market.

The MCA believes that the way it is approaching regulatory intervention is proportionate in the circumstances and justified in the light of the objectives as set out in the Framework. It also believes that the imposition of the above-mentioned set of remedies is the most appropriate in the current circumstances and the timeframe of this review. The MCA will continue to monitor developments in the market to ensure that it is applying justified remedies.

A Price control

In view of the risk of excessive pricing being applied by an SMP operator in the wholesale termination market, the MCA is of the opinion that cost orientation via a price control obligation should be imposed on SMP operators to efficiently address concerns on the pricing of termination.

This is in line with the EU Commission Recommendation on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU which states that 'NRAs should set termination rates based on the costs incurred by an efficient operator'.

A price control obligation upholding the principle of efficient FTRs has already been mandated on GO by virtue of its dominant (SMP) position designated under the previous

[16] This in accordance to Regulation 22 of the Electronic Communications Networks and Services (General) Regulations which authorises the imposition of such remedies.

market review carried out in 2006. The setting of FTRs (fixed interconnection rates)[17] is currently based on the MCA's Bottom-Up Cost Model ("BUCM")[18].

In view of the reconfirmation of GO's SMP status in the market under review, the current price control obligation on this operator is to be maintained.

The same price control obligation is also being mandated on Melita, SKY Telecom's SKYNet network, Vodafone (Malta) and SIS, given their SMP status in the provision of termination services.

The MCA requires that any rate(s) for wholesale termination are set equal to the efficient-operator rate established by the MCA's BUCM or any other means chosen by the MCA to set the efficient rates.

This ensures that the provision of access and interconnection to wholesale call termination services provided by all SMP operators is cost oriented, thereby allowing for efficient, fair, and reasonable termination charges.

The imposition of a price control obligation on all operators designated with SMP in this market review shall, in the first instance, take the form of an obligation mandating that the applicable wholesale termination rate(s) are set equal to the regulated 'efficient-operator' rate(s) established by the MCA. In addition, the MCA mandates that any changes to the regulated termination rates are reflected automatically in the RIO contracts.

In view of the new EU Commission Recommendation on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU (published in May 2009) the MCA is currently addressing the future regulatory strategy for fixed and mobile wholesale termination rates in Malta, with particular focus on the methodologies applicable in determining interconnection rates in line with the said EU Commission Recommendation. In this respect the MCA has already carried out a consultation exercise on the matter between November 2009 and January 2010[19].

The MCA has taken into consideration the three responses received and has now determined the interconnection strategy for the setting of the fixed termination rates. The interconnection strategy decision has been notified with this market review and will be published shortly.

B Cost accounting

The cost accounting obligation allows the MCA to monitor, on an ongoing basis, costs incurred by operators as opposed to the termination charges being applied, and ensures that fair, objective and transparent methodologies are followed by SMP operators in allocating costs to the regulated services.

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[17] The latest report published by the MCA setting fixed wholesale interconnection rates is found on the following link: http://www.mca.org.mt/infocentre/openarticle.asp?id=1338&pref=1

[18] The BUCM model has been developed in order to achieve the objective of gradually reducing the interconnection rates at efficient levels as outlined in the Interconnection Strategy for the Electronic Communications Sector published by the MCA in March 2005: http://www.mca.org.mt/infocentre/openarticle.asp?id=593&pref=1

The BUCM is based on a modified scorched-node approach which replicates an efficiently designed Next Generation Network. The underlying operating costs are adjusted to reflect the costs of an efficiently operated network, whilst the capital base is calculated using current costs. The model is constantly refined.

[19] http://www.mca.org.mt/infocentre/openarticle.asp?id=1377&pref=48

Information from such system will be used by the MCA to complement the application of other regulatory measures, such as transparency and non-discrimination.

Cost accounting data represents valuable information on the allocation of costs onto different services. This can also prove valuable in the eventuality of the development of a new cost model, even if this were to be based on a bottom-up methodology as, in practice, cost accounting data is used as reference or to calibrate the said model.

The MCA is imposing a cost accounting obligation on two operators designated with SMP in this market review, namely GO and Melita, as it does not consider the imposition of such an obligation to constitute an unreasonable burden on the said operators. This is necessary to effectively promote competition and curb possible abuse of dominance in the wholesale call termination markets identified in this review. Both GO and Melita are therefore obliged to support a cost accounting system as specified in the MCA decision on the *'Implementation of Cost Based Accounting Systems for the Telecommunications Sector'* published in July 2002[20].

The MCA must however consider that there are factors such as the size of the undertaking in the specific market, the share of the said undertaking in terms of the local subscriber base, its position vis-à-vis other competitors, and the time of entry in the market, which could determine the extent of the remedies to be imposed.

In view of the above, the MCA cannot ignore a clear difference in the market position occupied by the different operators designated with SMP in this market review. The MCA's approach to regulatory intervention must therefore be guided by the principles of proportionality and reasonableness to ensure that any remedial action corresponds with market realities.

In this regard, the MCA considers that it is not proportionate to impose a cost-accounting obligation on SKY Telecom, Vodafone (Malta), and SIS. This notwithstanding, the MCA will monitor developments in the identified markets and keep this approach under review. Amendments in this regard shall only be implemented following consultation with all interested parties.

The MCA also reserves the right to demand any information or data from SMP operators to ensure that they are not adopting pricing strategies that are disruptive to the market.

C Accounting separation

The MCA believes that effective monitoring of the transparency and non-discrimination obligations relies on the existence of accounting separation. In this regard, accounting separation facilitates the verification of compliance for services that FNOs provide to other operators.

Separated accounts help disclose possible market failures and provide evidence in relevant markets of the presence, or absence, of discrimination. These also support the imposition of transparency as it makes visible the wholesale prices and internal transfer prices of the operators' products and services. Separated accounts also allow the MCA to check compliance with obligations of non-discrimination and to address price competition problems.

Accounting separation also provides support to the price control obligation so as to ensure that wholesale prices are set in a transparent and non-discriminatory manner.

[20] Link to MCA Decision: http://www.mca.org.mt/infocentre/openarticle.asp?id=132&pref=1

The accounting separation obligation has already been mandated on GO by virtue of its dominant (SMP) position designated under the previous market review carried out in 2006. The MCA believes that this obligation is to be maintained on GO for the timeframe of this review. This obligation is now also being mandated on Melita.

The MCA believes that the imposition of an accounting separation obligation on both GO and Melita is appropriate in the current circumstances, given their size and market presence.

GO and Melita shall compile their separated accounts based on the guidelines issued in July 2009 (hereafter the "2009 Decision") on how the accounting separation obligation shall be implemented by telecoms operators.[21]

Based on the principles of reasonableness and proportionality, the MCA considers that, for the time being, it is not appropriate to impose an accounting separation obligation on the remaining SMP operators identified in this market review. Indeed, the imposition of an accounting separation obligation on SKY Telecom's SKYNet, Vodafone (Malta), and SIS would, at this point in time, be too onerous in view of their small customer base for voice services provided by the said operators.

The MCA also reserves the right to amend the current accounting separation obligation described above in accordance with its powers at law, in particular Regulation 20 of the ECNSR, and the principles of reasonableness and proportionality. Amendments in this regard shall be implemented following consultation with all interested parties.

4.4 Monitoring and reviewing of the markets

The MCA intends to keep a reasonably close watch on market developments to ensure that regulatory obligations on operators remain relevant within the two year timeframe of this market review. If the MCA deems necessary, an update to this market review or applicable remedies would be undertaken at any time in response to changes in market conditions.

[21] "Accounting Separation and Publication of Financial Information for Telecommunications Operators - Report on Consultation and Decision", MCA, October 2002
http://www.mca.org.mt/infocentre/openarticle.asp?id=323&pref=1

"Accounting Separation and Publication of Financial Information by Undertakings having SMP in the Electronic Communications Sector – Report on Consultation and Decision", MCA, July 2009
http://www.mca.org.mt/infocentre/openarticle.asp?id=1336&pref=13

DECISION 3

Approach to regulatory intervention

Given the position of dominance held by all SMP operators identified in this market review, and in light of potential competition problems that may arise, the MCA deems it necessary to impose the following obligations on the said operators, namely:

- Access to/and use of specific facilities;
- Non-discrimination;
- Transparency; and
- Price control.

The MCA is also mandating the obligations of accounting separation and cost accounting on GO plc and Melita plc.

The MCA's regulatory approach ensures that all remedial action is based on the nature of the competition problems that were identified, and that each obligation is proportionate and justified in light of the objectives set out in Article 4 of the Electronic Communications (Regulation) Act.

Appendix

UFFIĊĊJU TAL-PRIM MINISTRU

MALTA

OFFICE OF THE PRIME MINISTER

DIVIŻJONI TAL-KONSUMATUR
U TAL-KOMPETIZZJONI

Direttorat tal-Kompetizzjoni

CONSUMER AND COMPETITION
DIVISION

Competition Directorate

4th March 2010

The Chairman
Malta Communications Authority
Valletta Waterfront
Pinto Wharf
Floriana

Dear Chairman,

The Office for Fair Competition (OFC) has been asked to provide its opinion in respect of the Malta Communications Authority's (MCA) consultation document concerning the wholesale call termination on individual public telephone networks provided at a fixed location.

The OFC contends that the market assessment as conducted by the MCA follows standards that are in line with best practices normally used when defining relevant markets in competition analysis. The OFC considers that it is reasonable to accept for the period under review the MCA's identification and analysis of the wholesale call termination on individual public telephone networks provided at a fixed location in Malta. Nonetheless, MCA should continue to monitor market developments in this regard.

We would like to point out that our views are being submitted in the context of the specific provisions of the SMP guidelines relating to the relationship between markets defined for the purpose of ex-ante regulation vis-à-vis competition law enforcement. The OFC reserves the right to re-examine any or all of the issues underlying these MCA recommendations in the light of facts and evidence that may arise in specific future cases before it.

Yours sincerely,

Dr Mireille Vella
Director General

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