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Malta Communications Authority
(MCA)
Valletta Waterfront - Pinto Wharf
FRN 1913, Valletta
Malta

For the attention of
Mr. Edward Woods
Executive Chairman

Fax: +356 21 336 846

Dear Mr Woods,

Subject: Commission Decision concerning Case MT/2016/1957: retail and wholesale high-quality access provided at a fixed location in Malta

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

1. PROCEDURE

On 18 November 2016, the Commission registered a notification from the Maltese national regulatory authority, Malta Communications Authority (MCA)¹, concerning the retail and wholesale² markets for high-quality access provided at a fixed location in Malta.

The national consultation³ ran from 16 August to 30 September 2016.

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 The market for wholesale high-quality access provided at a fixed location corresponds to market 4 in Commission Recommendation 2014/710/EU of 9 October 2014 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 295, 11.10.2014, p. 79.

³ In accordance with Article 6 of the Framework Directive.

On 25 November 2016, a request for information⁴ was sent to MCA and a response was received on 30 November 2016.

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

2. DESCRIPTION OF THE DRAFT MEASURE

2.1. Background

The markets for retail and wholesale leased lines in Malta were previously notified to and assessed by the Commission under cases MT/2012/1386-1387-1388-1389-1390⁵.

At retail level, the MCA identified two relevant markets: i) the market for the provision of national dedicated capacity supplied over traditional interface ('TI')⁶ leased lines and Ethernet circuits, and ii) the market for the provision of international dedicated capacity supplied over TI leased lines and Ethernet circuits.⁷

At wholesale level, the MCA identified three relevant markets: i) the market for the provision of dedicated capacity over national trunk segments of leased lines; ii) the market for the provision of dedicated capacity over international trunk segments of leased lines; and iii) the market for the provision of dedicated capacity over terminating segments of leased lines.

All retail and wholesale markets were found to be national in scope.

Following the analysis of the three-criteria test, the MCA concluded that only the retail market for national leased lines, the wholesale market for national trunk segments of leased lines and the wholesale market for the provision of dedicated capacity over terminating segments of leased lines were susceptible to ex-ante regulation. The MCA designated the incumbent, GO, with significant market power (SMP) in the three markets.⁸

At retail level, the MCA imposed on GO a transparency obligation with regard to analogue national leased lines, while it imposed transparency and non-

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

⁵ C(2012) 9113.

⁶ Traditional leased lines include analogue and digital Synchronous Digital Hierarchy (SDH) leased lines.

⁷ The key functional difference between national and international leased lines lies in the location(s) to be served. An international leased line allows the end-user to establish a direct link to a foreign jurisdiction.

⁸ The MCA based its assessment on GO's market share (95.2% in terms of number of terminating segments of leased lines and 68.5 % in terms of revenues), the level of sunk costs, barriers to entry and potential competition, economies of scale and scope, the fact that infrastructure was not easily replicable, and vertical integration.

discrimination obligations with regard to digital SDH leased lines and Ethernet circuits. At wholesale level, the MCA imposed on GO the following obligations: (i) access, (ii) non-discrimination, (iii) transparency, (iv) accounting separation, (v) cost orientation, and (vi) cost accounting. The MCA withdrew all remedies from the markets which did not fulfil the three-criteria test.

The Commission commented on the existence of barriers to entry and the development of effective competition in the wholesale market for trunk segments, asking the MCA to closely monitor any market developments, as considerable market entry had already taken place. The Commission also urged the MCA to strictly enforce its wholesale regulation and to adjust it in the case it proved to be ineffective.

The price control obligation was effectively implemented in a subsequent notification (MT/2013/1480), which set the regulated charges for the different types of wholesale leased lines services according to a bottom-up model ('BUCM2'). The MCA indicated that the model would have to be adjusted at a later stage to remove the installation costs from the annual rental charges, to avoid double counting. The MCA was of the view that it would be disproportionate to delay further the application of the proposed lower prices until the BUCM2 was adjusted, especially given that the impact of the adjustment would be minor. The Commission commented on the need to update the model without undue delay.

2.2. Market definition

The MCA identifies a retail market and a wholesale market for the provision of high-quality access and connectivity services over national leased lines in Malta. On the basis of a substitutability assessment, the relevant retail and wholesale markets include leased lines provided over analogue, semi-digital, SDH, Ethernet and wavelength-division multiplexing (WDM) solutions. The regulator concludes that all bandwidths should be included in the same market, as a service with lower capacity or quality can always be substituted with a service with higher capacity or quality (the so-called chain of substitutability).

The relevant geographic market is national for both markets.⁹

2.3. Three-criteria test and finding of significant market power

2.3.1. Retail market

The MCA considers that the retail market for the provision of high-quality access and connectivity services over national leased lines does not fulfil the three-criteria test.

A number of alternative operators have entered the market for the provision of retail leased lines in Malta, namely Melita, Vodafone and Space Hellas.¹⁰ The MCA finds

⁹ All authorised operators providing retail and wholesale leased lines services in Malta are doing so without differentiating prices and availability on the basis of geographic location.

¹⁰ Cable operator Melita has a nationwide hybrid HFC/fibre network. Vodafone has deployed its own fibre network infrastructure (in selected parts of the island). Both are providing a diversified retail product portfolio via their respective networks. Space Hellas is purchasing wholesale leased line

that the presence of these providers, which mainly offer Ethernet leased lines, has had a material impact on the behaviour of the incumbent. The MCA concludes that the market is exhibiting a tendency towards effective competition.

GO's market share has fallen consistently over the past years due to increased competition from the other service providers.¹¹ GO is the only operator supplying TI leased lines in Malta and its loss of market shares should also be seen in the context of a steady decline of TI solutions, which are being replaced by Ethernet and, to a lesser extent, WDM lines.¹² The MCA believes that these trends will continue over the upcoming regulatory period, especially as GO will discontinue offers based on TI leased lines.

Finally, the MCA explains that the competitive situation at the retail level is linked to the wholesale market, for which the MCA is proposing ex-ante regulatory intervention (see below). The regulator explains that wholesale regulation is important to safeguard TI leased lines end-users, to ensure that GO does not use its market power to restrict the growth of newly-arrived service providers (such as Space Hellas) and for new market entry to occur.

Given that the retail market is showing a tendency towards effective competition and that no operator is deemed to hold SMP in the provision of retail leased lines services, the MCA proposes to remove the existing ex-ante regulation 90 calendar days after the publication of the final decision.¹³

2.3.2. Wholesale market

The MCA concludes that the wholesale market for the provision of high-quality access and connectivity services over national leased lines is not competitive and that GO continues to have SMP.

This preliminary conclusion is supported by a number of findings:

- There are high sunk costs that would have to be incurred by any service provider in order to fully replicate GO's access network infrastructure;

access (currently regulated) to provide high-quality access and connectivity services via national leased lines at the retail level.

¹¹ GO's retail market share in terms of revenues has decreased from 100% in Q1 2012 to 80% in Q1 2016. The market shares of Melita, Vodafone and Space Hellas stand respectively at 5.5%, 9.8% and 3.8% in Q1 2016.

¹² The number of leased lines provided over TI technologies has dropped from 521 in Q1 2012 to 133 in Q2 2016, while the number of Ethernet connections has increased from 309 to 395 in the same period. There are 6 WDM lines active at retail level.

¹³ The current regulatory regime in the provision of retail national leased lines is restricted to a light touch approach which features transparency and non-discrimination obligations. The MCA believes that the removal of these two measures would not impact the drive towards a more competitive retail market.

- GO enjoys persistently high market shares at the wholesale level¹⁴, particularly a 100% market share in the case of high-quality access and connectivity services supplied over wholesale national TI leased lines¹⁵;
- The incumbent's vertically and horizontally integrated structure makes it difficult for existing market players and new market entrants to compete with GO;
- The wholesale market exhibits a limited potential for new competition and expansion, given the small customer base and the lack of switching.

Therefore, in the absence of wholesale regulation, the MCA considers that GO could act independently of customers and other network operators in its wholesale pricing structure for the wholesale services under investigation. Hence, the MCA proposes to maintain regulatory measures to address these market shortcomings.

2.4. Regulatory remedies

The MCA proposes to maintain all wholesale ex-ante regulatory remedies which were imposed on GO in the previous market review, namely: i) provide access to/and use of specific network facilities; ii) transparency; iii) non-discrimination; iv) price control¹⁶, v) cost accounting; and vi) accounting separation.

3. COMMENTS

The Commission has examined the notification and the additional information provided by the MCA and has the following comment:¹⁷

Need to adjust the regulatory costing model

The Commission notes that the MCA has not yet proceeded to update the BUCM2 cost model, which as explained by MCA itself in the context of case MT/2013/1480, implies double counting of the installation costs in the annual rental charges. At the time, the MCA told the Commission that it intended to carry out adjustments to the model "as soon as possible".

The Commission takes note of the MCA's view that the resulting impact on the annual charges would not be significant and acknowledges that the model was not revisited due to resource prioritisation, as explained by the MCA in the response to the RFI.

¹⁴ GO's market share in Q1 2016 was 91% in terms of number of connections, including self-supply. If self-supply is excluded, GO's market share stood at 97% in Q1 2016, just down slightly from 100% in 2012.

¹⁵ It should be noted that, unlike the situation at retail level where Ethernet lines increasingly represent the preferred technology, TI leased lines are the most commonly sold type of lines at wholesale level, where TI lines are mainly purchased for voice interconnection.

¹⁶ The cost model BUCM2 will remain unchanged compared to the previous decision.

¹⁷ In accordance with Article 7(3) of the Framework Directive.

The Commission, however, urges the MCA to proceed to the adjustment of the BUCM2 model without delay. This is necessary to ensure, in general, that the regulated prices are set in a cost-oriented and transparent manner and, in particular, that wholesale leased lines prices resulting from the BUCM2 model accurately reflect the pricing structure envisaged by the MCA.

In the Commission's view, this is particularly relevant given the significant changes that have occurred in the wholesale market for leased lines since the development of the model currently in use, notably with the entry into the market of alternative operators and the steady migration of end-users from TI leased lines towards Ethernet and WDM-type connections.

The Commission's position on this particular notification is without prejudice to any position it may take *vis-à-vis* other notified draft measures.

Pursuant to Point 15 of Recommendation 2008/850/EC¹⁸ the Commission will publish this document on its website. The Commission does not consider the information contained herein to be confidential. You are invited to inform the Commission¹⁹ within three working days following receipt whether you consider that, in accordance with EU and national rules on business confidentiality, this document contains confidential information which you wish to have deleted prior to such publication.²⁰ You should give reasons for any such request.



Yours sincerely,

For the Commission,
Roberto Viola
Director-General

¹⁸ Commission Recommendation 2008/850/EC of 15 October 2008 on notifications, time limits and consultations provided for in Article 7 of Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services, OJ L 301, 12.11.2008, p. 23.

¹⁹ Your request should be sent either by email: CNECT-ARTICLE7@ec.europa.eu or by fax: +32 2 298 87 82.

²⁰ The Commission may inform the public of the result of its assessment before the end of this three-day period.