



JERSEY COMPETITION REGULATORY AUTHORITY

6th Floor, Union House, Union Street, St Helier, Jersey JE2 3RF
Tel.: +44 (0)1534 514990
Fax: +44 (0) 1534 514991
www.jcra.je

Consultation Document 2002/1
Issued by the JCRA

Market Definition & Significant Market Power in the Telecommunications Sector

In the consultation document ‘Telecommunications Licence Application Form 2002/TLA’ the JCRA stated that it would publish a consultation paper in due course on the meaning of Significant Market Power and Well Established Player. In this consultation paper the JCRA aims to set these concepts into the Jersey context.

The JCRA welcomes comments on any of the issues raised in the paper, although we would draw attention in particular to the key areas within the document where we have set out specific questions, which we would like consultees to address. (The questions arise throughout the paper and have been set out in bold italics.)

The JCRA looks forward to receiving your replies.

The deadline for comments is 28th March 2002.

Patrick McNutt
Chairman, JCRA

Charles Latham
Executive Director, JCRA



JCRA CONSULTATION

Market Definition & Significant Market Power in the Telecommunications Sector

**Consultation Document
2002/1
28th February 2002**

1. INTRODUCTION

The JCRA's policy objectives, in line with those in the UK and other European jurisdictions, are to promote and liberalise, where appropriate, services and associated facilities in telecommunications and to promote the interests of consumers. In the consultation document 'Telecommunications Licence Application Form 2002/TLA', the JCRA stated, in section 3.6, that it would publish a consultation paper in due course on the meaning of Significant Market Power (SMP) and Well Established Player (WEP). Undertakings found to have SMP and/or deemed to be a WEP will have sector specific obligations imposed on them so that their market power does not distort competition.

In the context of Jersey's telecommunications market, the JCRA is of the firm belief that any designation of undertakings with SMP and/or WEP includes the imposition, maintenance, amendment or withdrawal of specific regulatory obligations which relate to factors such as: transparency; non-discrimination; accounting separation; obligations for access to and use of specific network facilities; price control and cost accounting; retail tariff regulation; carrier selection and pre-selection and availability of leased lines.

In December 2001, the European Commission approved draft guidelines on market analysis and the calculation of significant market power in the context of electronic communications networks and services. Using the guidelines defined by the Commission and Oftel as representing best practice, this consultative paper aims to set the concept into the Jersey context.

Many electronic communication markets are fast moving and their structures are changing rapidly. The JCRA intends that the market analysis will be a forward-looking, structural, evaluation of relevant market(s) and that assessment should be ongoing with industry representatives. (Please go to Sections 3.5 & 3.6).

Following international best practice the JCRA is considering the organisation of an *Industry Forum* at the end of 2002 or as soon as possible thereafter. The purpose of such a Forum is to engage with all applicants in a public setting on the substantive, technical and accounting issues that have arisen during the consultation process on the provision of telecommunications in Jersey.

(Please note: definitions of the key technical terms contained within this paper may be referred to in Appendix 1).

Q 1.1: Do consultees agree that an Industry Forum should be arranged by the JCRA?

Q 1.2: Do you wish to participate in an Industry Forum?

2.0 MARKET DEFINITION

This paper also sets out to explain the concept of SMP and WEP. In order to make an assessment of SMP, it will be important for the JCRA to define the relevant market. The JCRA will draw upon recognised experience in the UK and in Europe.

The use of the term ‘relevant market’ implies a description of the products and services that make up the market and the assessment of the market’s geographical scope. The JCRA is of the view that a dynamic rather than static approach is required when carrying out a prospective market analysis.

2.1 The relevant product/service market

The relevant market comprises all those products or services that are sufficiently interchangeable or substitutable. Products or services, which are only to a small or relative degree interchangeable with each other, do not form part of the same market.

There are two main competitive constraints to consider:

(i) The extent to which consumers are prepared to substitute other services or products for the service or product in question (demand-side). In determining the existence of demand-side substitutability, the JCRA will make use of any previous evidence of consumer’s behaviour such as historical price fluctuations in potentially competing products; records of price movements, and/or relevant tariff information. Evidence shows that consumers have in the past shifted to other products or services, in response to past price changes.

Switching costs is another factor that may hinder consumers ability to substitute a product or service and the JCRA intends to give this important element due consideration.

(ii) The extent to which suppliers other than those offering the product or service would switch their line of production without incurring significant additional costs. Entry should be credible, feasible and likely to occur within a reasonable time-frame. Supply-side substitution may serve not only for defining the relevant market but also for identifying the number of market participants. In assessing the scope of supply-side substitutability, the JCRA will ascertain whether a given supplier would actually use or switch its productive assets to produce the relevant product or offer the relevant service (for instance, whether their capacity is committed under long-term supply agreements).

The JCRA would also take account of any existing legal, statutory or other regulatory requirements, which could defeat a time-efficient entry into the relevant market and as a result discourage supply-side substitution. A third source of competitive constraint on an operator’s behaviour is potential competition. The JCRA will take account of all arguments presented by consultees on the scope and extent of potential competition in the relevant markets in Jersey.

2.2 Geographic Market

The geographic market is an area in which 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. Markets can be global, pan-European, national or even island-specific in scope. On the other hand, markets can also be defined on a route-by-route basis.

Q 2.2.1: Do consultees agree that the JCRA should follow best practice from Europe where the telecommunications sector has been defined in a number of relevant markets?

Essentially there are at least two main types of relevant market within the telecommunications sector, namely services provided to end users (or services market) and that of access to facilities necessary to provide such services (or access to infrastructure market). Within these two broad market definitions, further market distinctions may be made depending on demand and supply patterns. In addition a further distinction exists between wholesale and retail markets which arises out of differences in pricing models and offerings for a given product or service.

Q 2.2.2: Do consultees agree with the market definitions?

Although physical characteristics can be important, it should be remembered that different kinds of products or services may be used for the same end. For instance, customers may use dissimilar services such as cable and satellite services connections for the same purpose, namely access to the Internet. In such a case, both services may be in the same product market. Conversely, paging services and mobile telephony services, which may appear to be capable of offering the same service, that is, dispatching two-way short messages may be found to belong to distinct product markets in view of the different perceptions by consumers as regards their functionality and end use.

Q 2.2.3: Do consultees agree with the identification of a product and a geographic market in accordance with European (and UK) best practice?

2.3 Following International Best Practice

The JCRA will be alert to the possibility that product substitutability between different electronic communications services may arise through the convergence of various technologies. A prime example of such convergence is the packet-switched network, used in the Internet, which may also be used to transmit digitised voice signals in competition with traditional voice telephony services.

As regards the fixed services market, the European Commission has defined the relevant market as being the market for domestic and international voice and data communications services, with further segmentation between the voice market (in which both private households and business customers participate) and the data market (primarily used in business). In the market for fixed telephony retail services, the Commission has distinguished various services: the initial connection, the monthly rental, local calls and long distance calls. With regard to mobile communications, from the demand-side point of view, mobile services and fixed telephony services constitute separate markets.

In the telecommunications market, the existence of the following main markets is now acknowledged:

- International voice-telephony services
- Advanced telecommunications services to corporate users
- Standard low-level packet switched data-communications services
- Resale of international; transmission capacity
- Audio conferencing
- Satellite services
- Enhanced global telecommunications services
- Directory assistance services
- Internet-access services to end users
- Seamless pan-European mobile telecommunications services to internationally mobile customers

Q 2.3.1: Do consultees believe that the criteria outlined above and the list of the main telecommunications markets, is a suitable starting-point for the JCRA?

A distinction should be made between the provision of infrastructure to other operators (wholesale level) and provision to end users (retail level). The latter is further sub-divided between business and residential customers.

In the case of the mobile market, an important distinction should be made between two different markets (i) access for fixed operators to mobile markets (wholesale charges for call termination) and (ii) provision of mobile services to end users (retail market).

Q 2.3.2: Do consultees agree that the JCRA should be influenced by these market distinctions?

3.0 DETERMINING SMP

3.1 Fixed Public Telephone Network and Services

The JCRA proposes that shares of the market for voice telephony services should be assessed on the basis of retail revenues excluding the revenues related to the

supply of terminal equipment. Shares of retail revenues provide a simple and reasonably effective measure of retail market power. The JCRA is of the view that it is best to use revenues from terminating calls to calculate market shares for both fixed public telephony networks and services. This measure should include a notional value for self-terminated own-network traffic and the termination of interconnection traffic received from other networks.

Q 3.1.1: Do consultees agree with this view?

3.2 Mobile Public Telephone Network and/or Services

For determining shares of the mobile public telephony network and/or services the JCRA proposes to use the same approach as in the fixed public telephony networks, that is, the revenues from terminating calls. This measure should also include a notional value for self-terminated own-network traffic and the termination of interconnection traffic received from other networks.

3.3 Leased Lines

In common with best practice, the JCRA proposes that for the purposes of leased lines, that shares of the leased lines market be measured in terms of shares of revenues from customers (be they domestic or business customers or other operators).

3.4 The National Market for Interconnection

An assessment of SMP in a national market for interconnection is required. The JCRA is of the view that market shares are best measured by call termination revenues. Call termination revenues are calculated by way of a two-stage test. The first stage is in the same way as for the fixed and mobile public telephone network/services markets, namely including:

- Calls terminating on networks (including fixed public telephony networks, mobile public telephony networks and leased lines) within Jersey regardless of their origin;
- An imputed value for self-terminated calls; but excluding traffic conveyed but not terminated by operators.

Q 3.4.1: Do consultees agree that this procedure is appropriate for the determination of SMP in the interconnection market in Jersey?

The second stage analysis requires:

- The identification of economic markets lying within (or crossing the boundaries of) the national market for interconnection;
- Consideration of competitive conditions within these markets on a forward-looking basis.

The market in Jersey for interconnection might consist of a wide range of network services of different types. In particular, interconnection services supplied by fixed operators could be differentiated according to the level of the network at which interconnection is provided. It is possible therefore to distinguish (at least) between double tandem interconnection, single tandem interconnection and primary interconnection (call termination). These fixed interconnection services are likely to be of limited substitutability on either the demand or supply side.

However, with respect to interconnection with mobile, by the very nature of a mobile network, it might not be currently possible for an interconnecting operator to self-supply some of the conveyance and switching activities that a mobile operator undertakes. This might arise because the location of the mobile customer is not known to the originating operator. Thus, mobile interconnection services are provided as a single undifferentiated bundle and cannot at present be unbundled.

Therefore, the JCRA proposes not to pursue an examination of unbundled stage 2 markets at this juncture until further analysis is undertaken into mobile interconnection services on the island and the extent to which they may be incapable of being unbundled at present. However, the JCRA also recognises that technological and market circumstances may change to allow this analysis to be carried out.

Q 3.4.2: Do consultees agree:

(i) with a two stage approach?

(ii) not to apply such an approach to mobile interconnection?

3.5 Forward-Looking Assessment

A forward-looking assessment of competitive conditions

Any forward-looking approach to the assessment of market power requires that: market trends are assessed to see whether an operator's current market power is greater than or less than that suggested from Stage 1 market shares computed from historic data; and the extent to which any market power exercised in the Jersey market for interconnection is transient or likely to endure for some time.

The assessment of the transience of market power in the interconnection market may be influenced by a number of non-exhaustive factors including:

- The development of fixed to mobile traffic.
- The impact of the introduction of new operators into the market.
- The trend in mobile termination rates.

A forward-looking assessment of Interconnection Agreements

The JCRA would envisage that JT will enter into interconnection agreements with those applicants intent on using the JT network, with their own switches and billing system.

The JCRA intends to publish its 'Standard List of Interconnection Services' after consultation with JT and other applicants; this is expected by June 2002. The interconnection services will include those, which the JCRA believes should be on JT's initial standard list in their licence application. Through the auspices of Article 22 the JCRA is prepared to facilitate an arbitrated solution to interconnection that can be voluntarily agreed to by all parties.

Q 3.5.1: Do consultees agree with this approach?

Q 3.5.2: Should the industry await the publication of an RIO (Reference Interconnect Offer) from JT?

3.6 Well-Established Player (WEP)

The JCRA is of the view that the standard of well-established player may be appropriate in the early stages of liberalisation of telecommunications in Jersey. A well-established player (**WEP**, henceforth) is an obligatory partner in the market and will be in a market position that enables it to command a role of 'gate-keeper' in the provision of telecommunications services. A WEP may also be defined with respect to the ownership of an underlying public infrastructure or public telecommunications network¹ deemed to be an essential facility.

The JCRA licensing structure will allow the JCRA:

- (i) To impose obligations and requirements on a licensee relating to the mandatory provision of publicly available telecommunications services and/or public telecommunications infrastructure and/or public telecommunications network, including obligations which require the licensee to provide universal service and other obligations; and
- (ii) To impose specific obligations where the licensee has SMP and/or is a well established player.

The JCRA's adoption of a WEP standard is based on the premise that it may be judicious in an island economy like Jersey to make a distinction between market players operating on the basis of their own infrastructure and those operating on the basis of leased capacity. Under this approach our minimal regulatory framework would govern all players in the telecommunications sector deemed to have SMP and WEP status. In addition a developed set of rights and obligations would apply to those firms providing a public infrastructure or public telecommunications network or publicly available services.

¹ Under EU law, networks built from leased lines (that is, capacity leased from a third party) do not appear to count as telecommunications networks proper, but are rather seen as an incident of service provision. The JCRA is mindful of the dispute between the German regulator, RegTP and the Commission on the definition of a 'public network'. They agreed that a network with a minimum of one switch and three lines could be defined as a public network.

In substantive terms, this approach contains fairly detailed sets of provisions concerning central topics such as USO (both its scope and financing), interconnection, interoperability and licensing. The JCRA is of the view that interconnection is a key element of a fully liberalised market. The JCRA's principles are that interconnection² between a public infrastructure and services must be ensured, and that operators with SMP and/or WEP status must grant access to their public infrastructure or public telecommunications network and respect the principles of non-discrimination, proportionality, transparency and objectivity.

The JCRA might have to consider not only the ability of operators to influence market conditions, but also additional factors such as:

- The turnover of the organisation concerned;
- The control exercised or capable of being exercised by the organisations concerned of the means of access to end-users;
- The access to financial resources of the organisations concerned;
- The experience of the organisations concerned in providing products and services in the market.

Based on these tests outlined above, a typical incumbent PTO, as the current monopoly provider, would qualify as a WEP and is likely to have significant market power.

Q 3.6.1: Do consultees agree with this approach?

4.0 CALCULATING SMP

The JCRA believes that a finding of SMP may not be incompatible with some competition in the market. In an *ex-ante* environment, market power is essentially measured by reference of the power of the undertaking concerned to raise prices by restricting output without incurring a significant loss of sales or revenues. Often the lack of evidence or of records of past behaviour or conduct will mean that the market will have to be based on a prospective assessment.

The market power of an undertaking can be constrained by the existence of potential competitors. The JCRA wishes to use a clear and demonstrable benchmark for the assessment of market power. The criteria for assessing SMP could be based on market shares. A market share test is seen as providing such a benchmark. For example, in the UK, where the shares are greater than 25%, this will often be used as a proxy for market power.

In addition, if an undertaking's market share has remained stable over time, there could be a presumption of SMP. On the other hand, if market shares fluctuate over time, this may be indicative of a lack of market power in the relevant market. Finally a loss of market share may indicate that the market is becoming more

² As determined by best practice from European Directives, particularly the earlier Directive 97/33 as well as Directive 92/44 and Directive 98/10 and the new Framework.

competitive. 'Barriers to entry' can also be used as a means to measure market share. In the telecommunications sector, barriers to entry are often high because of existing legislative requirements (e.g. planning permission), which may limit the provision of certain services. Furthermore barriers to entry exist where entry requires large investments and the programming of capacities over a long time in order to be profitable.

4.1 Methods for Market Measurement

The criteria to be used to measure the market share of the undertaking(s) concerned will depend on the characteristics of the relevant market. Both volume sales and value sales provide useful information as methods for market measurement. Other criteria can also be used to measure market power include:

- Overall size of the undertaking
- Control of infrastructure not easily duplicated
- Technological advantages or superiority
- Absence of countervailing buying power
- Easy or privileged access to capital markets/financial resources
- Product/services diversification (e. g. bundled products or services)
- Economies of scale
- Economies of scope
- Vertical integration
- A highly developed distribution and sales network
- Absence of potential competition

Q 4.1.1: Do consultees agree and on what basis might they agree or disagree?

The JCRA suggests for example that leased lines revenues, leased capacity or numbers of leased line termination points are possible criteria for measuring an undertaking's relative strength on leased lines markets.

Q 4.1.2: Do consultees agree?

A suitable measurement parameter for interconnection would be the revenues accrued for terminating calls to customers on fixed or mobile networks. The use of revenues, rather than for example call minutes, takes account of the fact that call minutes can have different values (i.e., local, long distance and international) and provides a measure of market presence that reflects both the number of customers and network coverage. The use of revenues for terminating calls to customers of mobile networks may be the most appropriate means to measure the market presence of mobile network operators.

Q 4.1.3: Do consultees agree?

5.0 OLIGOPOLY / COLLECTIVE DOMINANCE

The notion of oligopoly or collective dominance is increasingly important in European Commission thinking. The European Commission has applied the concept of collective dominance in relation to oligopolistic markets where market structure has been considered conducive to co-ordinated effects.

Q 5.0.1: Should the JCRA go down this route?

The European Commission has relied upon a certain number of criteria, which can be summarised as follows:

- Few market players
- Mature market
- Stagnant or moderate growth on the demand side
- Low elasticity of demand
- Homogeneous product
- Similar cost structures
- Similar market shares
- Transparent market conditions
- Lack of technical innovation, mature technology
- Absence of excess capacity
- High barriers to entry
- Lack of countervailing buying power
- Lack of potential competition
- Various kind of informal or other links between the undertakings concerned
- Retaliatory mechanisms
- Lack or reduced scope for price competition.

In the telecommunications sector, an operator with a dominant position on the infrastructure market often has significant presence on the downstream, services market. The JCRA proposes to consider viewing two or more players in a market as being in a collectively dominant position. However, the JCRA will develop its own tests and consider the relevancy of the concept to an island economy.

Q 5.0.2: Do consultees believe that there is scope for viewing two or more players as being in a collectively dominant position?

6.0 Conclusion

In conclusion, Respondents are requested to comment on the matters set out in sections 1 through to 5 of this paper. It would assist in the consideration of responses if the question numbers in the above sections were quoted in any replies.

ENDS

Definitions

Interoperability – the possibility of connection of two telecommunications systems whereby information is mutually passed between them.

Interconnection – connection of two telecommunications systems for the purpose of passing traffic.

Traffic – the sending of calls or data across a telecommunications network.

Terminating calls – calls successfully connected on a telephone network.

Tandem connections – the process whereby calls are connected through a telecommunications network but not terminated on that network.

Single tandem – calls passed through a network B from operator A to operator C.

Double tandem – calls passed through a network which are already in tandem from another network, i.e. A – B – C – D where A is the originating operator and D is the terminating operator.

Self-terminating traffic – traffic passed through a network from a terminal on that network to another terminal on the same network

USO – Universal Service Obligation – a minimum configuration, agreed with the regulator, which the operator must supply if requested by a customer.