

Appendix A



POST AND TELECOM
ADMINISTRATION
IN ICELAND

Market analysis of the retail market for minimal set of leased lines (former Market 7)

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Summary and Conclusions

This document contains a draft by the Post and Telecom Administration (PTA) of analysis of the retail market for minimum set of leased lines, which is Market 7 in the older ESA Recommendation on the relevant market from 14 July 2004. The market analysis is the basis for decisions on whether to impose, maintain, amend or withdraw specific regulatory obligations on electronic communications undertakings that have been designated as having significant market power.

An analysis of this market was previously made in the year 2007. The conclusion of that analysis was that Siminn had significant market power and obligations were imposed on the company for:

- The provision for lease of specific types of lines
- Non-discrimination
- Transparency
- Accounting separation
- Price control (cost analysis based on historical cost)

The PTA has now made a new analysis of the relevant market. As this market is no longer listed in the said ESA Recommendation from 2008 it is necessary to evaluate whether it still fulfils the conditions required for possible implementation of ex-ante obligations. The criteria that the market needs to fulfil are in the first case that there are high and non-transitory barriers to entry, in the second case that the market is not tending towards active competition and in the third case that the implementation of general rules of Competition Law will not suffice on their own to address the failures of the market.

The PTA conclusion is that the market is no longer characterised by high and non-transitory barriers to entry and that this market thus does not fulfil all the necessary conditions for the imposition of ex-ante obligations. In addition to this the PTA points out that obligations on wholesale markets for leased lines should in the opinion of the EU Commission suffice on their own to establish effective competition on the relevant markets.

In the light of the above conclusion of analysis of the market, the PTA intends to withdraw the designation of Siminn as an undertaking with significant market power on the market and furthermore to withdraw the obligations that were imposed on Siminn on this market with the PTA Decision no. 20/2007 of 14 September 2007.

PTA will continue to closely monitor developments on this market and should circumstances change significantly then the Administration will evaluate the need for a new analysis of the market.

1.0 Introduction

1.1 General

1. This document presents the Post and Telecom Administration (PTA) analysis of the retail market for minimum set of leased lines¹. The PTA published an analysis of this market, along with its Decision on obligations on undertakings with significant market power on 14 September 2007. It is assumed that market analyses will be repeated at regular intervals in order to monitor whether circumstances have changed on the market.

2. This document is based on the draft PTA Decision on the market in question that were submitted for consultation on 27 November 2013, where electronic communication undertakings, the Competition Authority and other stakeholders were invited to comment on the market analysis and its conclusions; see Article 6 of Act no. 69/2003 on the Post and Telecom Administration. The consultation was closed on 20 January 2014. The Competition Authority and Fjarskipti hf (Vodafone) submitted comments where both parties stated that they agreed with the conclusions of the analysis. This strengthens the conclusions of the PTA. Market analysis and the draft decision with respect to obligations on the relevant market is now sent to the EFTA Surveillance Authority (ESA) for consultation pursuant to paragraph 1 of Article 7 of the same Act. Should ESA make no comments on the analysis and on the PTA draft Decision then the PTA Decision will be notified to the companies in question.

1.2 Electronic communications legislation

3. The Electronic Communications Act number 81/2003 implements the European Union (EU) Directives on Electronic Communications.² EU electronic communications legislation is intended to create a homogenous working environment for electronic communications undertakings in Europe, to limit barriers to entry and create conditions for sustainable competition for the benefit of consumers.

4. Pursuant to Chapter V of The Electronic Communications Act the PTA is obliged to define certain electronic communications markets, both in terms of service and in terms of geographical scope, in accordance with the fundamental principles of Competition Law and the obligations pursuant to the European Economic Area (EEA) Agreement. Furthermore, the PTA is required to analyse the defined markets and determine whether they are characterised by active competition. If the PTA comes to the conclusion that there is active competition in the relevant market – i.e. that no operator has SMP – it is prohibited from imposing obligations on the operators in that market. If the Administration has previously imposed obligations on undertakings in the relevant market, these shall be withdrawn and no new obligations imposed. Should on the other hand, the PTA come to the conclusion that

¹ Market 7 in the ESA Recommendation on the relevant market from 2004 which is now no longer in force.

² Directive of the European Parliament and Council no. 2002/19/EC from 7 March 2002 on access to and interconnection of electronic communications networks and associated facilities (Access and Interconnection Directive)

Directive of the European Parliament and Council no. 2002/20/EEC from 7 March 2002 on the provision of authorisation for electronic communications networks and service (Authorisation Directive).

Directive of the European Parliament and Council no. 2002/21/EC 2002/21/EC, of 7 March 2002, on a common regulatory framework for electronic communications networks and services (Framework Directive).

Directive of the European Parliament and Council no. 2002/22/EC from 7 March 2002 on universal services and users' rights relating to electronic communications networks and services (Universal Service Directive).

competition is not active on the relevant market because one or more undertakings have significant market power, then the Administration is obliged to designate them as having significant market power and to impose on them the appropriate obligations. According to Article 7 of the Act on the Post and Telecom Administration, the PTA is obliged to consult with ESA and with other electronic communications regulatory bodies in the EEA area on the definition of markets, market analysis and on decisions on obligations.

5. The European Commission has published Guidelines and a Recommendation for market analysis. On the one hand there are Guidelines on market analysis and assessment of SMP³ and on the other hand there is a Recommendation on the relevant markets.⁴ The EFTA Surveillance Authority (ESA) has issued analogous Guidelines⁵ (hereinafter called “the Guidelines,”) and a Recommendation⁶ (hereinafter called “the Recommendation”) and the PTA has taken into account both to the Guidelines and Recommendations from ESA and from the Commission when conducting its market analyses.

6. In the existing Recommendation on the relevant market, seven electronic communications markets that the PTA is obliged to analyse have been defined, in accordance with current electronic communications legislation and with Iceland's obligations pursuant to the EEA Agreement. Furthermore the electronic communications legislation prescribes that the PTA define these markets in accordance with circumstances that pertain in Iceland. Given the above it could transpire that the PTA market analysis will deviate from what is prescribed in the Recommendation.

7. In a prior ESA Recommendation from 2004, 18 markets were specified including the retail market for minimum set of leased lines. This market is not to be found in the current Recommendation which means that it has to be particularly examined in the light of circumstances pertaining in this country as to whether it still meets the criteria to be susceptible to ex-ante obligations according to Chapter 7 of the Electronic Communications Act.

8. The Ministry of Communications has issued a Regulation on market analysis in the

³ Commission Guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic networks and services, 2002/C 165/3.

⁴ Existing regulations are: Commission Recommendation of 17 December 2007 on relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services (notified under document no. C(2007) 5406) (2007/879/EC) and explanatory notes;

Commission Staff Working Document - Explanatory Note Accompanying document to the Commission Recommendation on Relevant Product and Service Markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services (Second edition) {(C(2007) 5406)}

⁵ EFTA Surveillance Authority Guidelines of 14 July 2004 on market analysis and the assessment of significant market power under the regulatory framework for electronic communications networks and services referred to in Annex XI of the Agreement on the European Economic Area.

⁶ Existing regulations are: EFTA Surveillance Authority Recommendation of 5 November 2008 on relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with the Act referred to at point 5cl of Annex XI to the EEA Agreement (Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communication networks and services), as adapted by Protocol I thereto and by the sectoral adaptations contained in Annex XI to that Agreement.

field of electronic communications, no. 741/2009, with the authority of Paragraph 3, of Articles 18 and 75 of the Electronic Communications Act. The Regulation covers the process and the main criteria to be applied when defining electronic communications markets, analysing relevant markets, making Decisions on designation of an undertaking or undertakings as having significant market power and making decisions on obligations according to the Electronic Communications Act no. 81/2003. The Regulation is based on the above specified EU Instruments, Recommendations and Guidelines.

1.3 The PTA's execution of market analysis

9. All things being equal, the implementation of market analysis can be divided into three phases:⁷

1. Define the relevant service markets and geographical markets.
2. Analyse the defined markets, determine whether there is active competition on these markets and make a Decision on whether one can find one or more undertakings with significant market power in a market.
3. Make a decision on whether obligations shall be imposed, maintained amended or withdrawn on undertakings with SMP.

10. With respect to these markets that are no longer in the ESA Recommendation, it further needs to be evaluated whether the market still fulfil the conditions to be susceptible to the imposition of ex ante obligations (the 3 criteria test). The criteria in question are the follows:

1. High and non-transitory barriers to entry to the market.
2. The market is not tending towards active competition.
3. The implementation of general rules of Competition Law will not suffice on their own to address the failures of the market.

11. This market analysis is based among other things on replies from parties to the market to a questionnaire that was distributed 18 June 2012. The Administration has collected information, inter alia regular statistical information, and has had informal communications with parties to the market. Statistics are collected from all parties to the market at 6 monthly intervals. In addition to this, the PTA collects and registers information on all changes to tariffs as they take place.

12. A preliminary draft of this analysis was sent to the Competition Authority and to stakeholders and they were asked to make comments. The PTA processed the comments received. As comments were only received from 2 parties, Competition Authority and Vodafone, and as both parties declared they agreed with the analysis then the comments will not be dealt with in a separate document. The market analysis and draft Decision with respect to obligations on the relevant markets will now be sent to the EFTA Surveillance Authority (ESA) for consultation; see Paragraph 1 Article 7 of Act no. 69/2003 on the Post and Telecom Administration. Should ESA make no comments on the market analysis and on the draft PTA Decision then the Decision will be notified to the companies in question.

1.4 General on the definition of markets

13. According to Article 16 of the Electronic Communications Act no. 81/2003 as amended, the PTA shall define service or product and geographical markets in accordance with the main principles of Competition Law and with obligations pursuant to the EEA Agreement. As has been stated it is necessary for the PTA to evaluate whether the markets, as defined in the Recommendation, harmonise with Icelandic circumstances. Both the service

⁷ See further in: "PTA information brochures on market analysis. Last updated in August 2009. [http://www.pfs.is/upload/files/Kynningarrit_um_markaðsgreiningu_ágúst_2009\(1\).pdf](http://www.pfs.is/upload/files/Kynningarrit_um_markaðsgreiningu_ágúst_2009(1).pdf)"

and geographical markets must be defined before it is possible to assess whether market conditions are such that they are susceptible to the imposition of ex-ante obligations.

14. In Article 4 of the Competition Act no. 44/2005 a market is defined as a sales area for a product and substitute product and/or a sales area for a service and substitute service. Substitute products and services are defined as products or services that can, wholly or to a significant extent, take the place of other products or services not only on the basis of the objective characteristics of the product in question, the purchaser's intended use of them and their price, but also with respect to competition requirements and/or conditions relating to supply and demand. Products that can compete with one another are therefore called substitutable products, and each market consists of products that are mutually substitutable. Products that can be substituted for one another only to a limited extent are not considered to belong to the same market.

15. Substitutability is assessed from two points of view. First, how readily customers believe that one product can be a substitute for another (demand-side substitutability). Second, how easily a competitor of a given undertaking can adapt his production so that his product falls within the market to which a product of the given undertaking belongs (supply-side substitutability).⁸ Demand-side substitutability is considered fundamental to market definition, while supply-side substitutability is less meaningful and is often related instead to an assessment of potential competition.

16. When a service market has been defined, its geographical dimension must be defined.⁹ The main rule is that it is based on the scope of the electronic communications network and the legislative jurisdiction of the regulatory framework that applies to it. Geographical demarcation is also based on an assessment of substitutability of the product or service in question, on the supply side and on the demand side. The geographic market is the area where products or services are offered on sufficiently homogeneous competitive terms. In assessing demand-side substitutability, it is appropriate to consider customers' taste and geographical purchasing patterns. On this basis it is possible to define markets as local, regional, national, or transnational; i.e. extending to more than one country. If a market is considered to extend to more than one country, European regulatory authorities collaborate on the market definition together with the European Commission and ESA, if appropriate.

⁸ See further Paragraph 39 in the Guidelines and the Explanatory Memorandum the EU Commission Recommendation, Chapter 3.1.

⁹ Definition of the geographical dimensional of markets is discussed in Chapter 2.2.2 of the ESA Guidelines and also in the COMMISSION NOTICE on the definition of the relevant market for the purposes of Community competition law. (OJ C372 9/12/1997) and ERG Common Position on Geographic Aspects of Market Analysis (definition and remedies) - October 2008 ERG (08) 20 final CP Geog Aspects 081016.

2.0 Definition of service markets for the minimum set of leased lines.

2.1 Definition in the ESA Recommendation

17. The service market here being examined is defined in ESA Recommendation on the relevant market from 14 July 2004, which is now no longer in force. This is Market 7 in the Annex to the Recommendation and was defined in the following manner:

The minimum set of leased lines (which comprises the specified types of leased lines up to and including 2Mb/sec as referenced in Article 18 and Annex VII of the Universal Service Directive).

This market is referred to in Annex I(1) of the Framework Directive in respect of Article 16 of the Universal Service Directive (the provision of leased lines to end users).

18. The PTA made reference to the ESA definition and the Explanatory Notes to the EU Commission Recommendation for the relevant markets when making its analysis in the year 2007.

2.2 The PTA definition of the relevant service markets

19. In its analysis of Market 7, which was published with the final edition of the PTA Decision no. 20/2007, dated 14 September 2007, the PTA defined the retail market for minimum set of leased lines. This definition is based on the definition in the ESA Recommendation from 2004 that was then in force, taking into consideration the Explanatory Note to the EU Commission Recommendation then in force.

20. In addition to the items mentioned in the definition in the Recommendation, the PTA described further characteristics of market 7 in more detail in its analysis from 2007 in the following manner:

21. The market covered the offer of leased lines to users. Users were those who used the service for their own requirements and who did not use it as procurement from electronic communications companies for resale.

22. The PTA defines leased lines as dedicated transmission capacity of signals between predefined points. Leased line markets did not cover switching of lines, i.e. a service which allows the user to decide varying destinations for the transmission of signals in each instance that they are sent. A service which connects one network connection point with many could on the other hand be considered a leased line if all points were predefined when the service is set up.

23. The definition of leased lines was independent of technology and transmission media but however the defined retail market only covered lines with up to 2 Mb/s transmission speed which meant that technical solutions that allowed for greater transmission speed would normally not be on this market.

24. The minimum set of leased lines comprised the following types according to the

decision of the EU Commission from 24 July 2003 – (2003/548/EC):

Analogue lines for voice, 2 wire

Analogue lines for voice, 4 wire

Digital lines 64 Kb/s

Digital lines 2 Mb/s

25. The leased lines on offer at retail on the domestic market that the PTA considered to be within the definition can be seen in table 2.1.

Table 2.1 Lines that belong to the retail market for the minimum set of leased lines

Lines for data transmission without endpoint devices	Analogue lines within areas	Digital lines between or within a telephone exchange areas with endpoint devices
Leased lines, 2 wire without endpoint devices	Analogue line, 2-wire line for voice	Digital line 64 Kb/s
Base line, 4 wire without endpoint devices	Analogue line, 4-wire for voice	Digital line 128 Kb/s
		Digital line 256 Kb/s
		Digital line 512 Kb/s
		Digital line 2 Mb/s

26. The PTA came to the same conclusion as the Commission that it was unnecessary to extend the limits for capacity beyond 2 Mb/s for the minimum set of leased lines.

27. The PTA considers that the definitions of the markets that were used in the year 2007 still apply and will use them in this analysis.

3.0 Definition of geographical market

28. A geographical market covers a geographical area where stakeholder companies participate in supply and/or demand of the relevant goods or services where conditions for competition are the same or sufficiently homogenous and where it is possible to demarcate the geographical area from neighbouring area where conditions for competition are significantly different. In assessing demand-side substitutability, it is appropriate to consider customers' taste and geographical purchasing patterns. It is customary to demarcate geographical electronic communications markets with reference to the distribution of the relevant electronic communications networks and to the jurisdiction of the legal framework that applies to the relevant market.¹⁰ ERG (now BEREC) has issued Guidelines that constitute a joint position on various aspects relating to the geographical division of markets.¹¹

29. In accordance with the ESA Guidelines one must take into account and define the market as that geographical area where the product in question is offered to customers with similar and sufficiently homogenous competition conditions. When markets are defined geographically it is not necessary for competitive conditions of electronic communications companies to be exactly the same. It suffices that they are similar or sufficiently alike and for this reason it is only areas where competition circumstances are really "different" that cannot be considered to be the same geographical market.

30. Among the significant factors when assessing geographical markets are the nature and characteristics of the product or service in question, possible entry barriers and/or customer behaviour, the number of service providers, a clear difference in market share of companies in the area in question and surrounding areas or a significant price difference between areas. Then one can examine whether there is a difference in marketing and/or quality of service between geographical areas.

31. In its analysis of the market in 2007 the PTA came to the conclusion that the whole country was one market. The PTA considers that this delineation still applies. The PTA considers that the changes that have taken place on the markets since 2007 are not such that they would warrant dividing the country into smaller market areas.

32. The Siminn electronic communications network and the Mila underlying network reach almost all homes and companies in the country and the price is the same throughout the country. The scope of companies other than Siminn on the market does not warrant a narrower delineation of the market. One must take into account that price on the market is independent of location, that the jurisdiction covers the whole country and that a narrower delineation would not impact the main conclusions of the market analysis. In the opinion of the PTA, it is not possible to delineate an area where conditions for competition are significantly heterogeneous to that which applies elsewhere in the country. The PTA further considers that there is no difference in preferences or purchasing pattern of users by region. Service providers have additionally not limited their services on this market to specific regions.

¹⁰ See Chapter 2.2.2 in the Guidelines.

¹¹ ERG Common Position on Geographic Aspects of Market Analysis (definition and remedies) - October 2008 ERG (08) 20 final CP Geog Aspects 081016.

33. In the light of this fact the PTA considers that the country is one geographical market for the retail market for minimum set of leased lines.

4.0 Conclusion of Market Analysis from 2007

34. In 2007 when the prior market analysis was published there were 4 companies operating as sellers on the relevant market; Siminn, Fjarski, Tengir and Vodafone. Of these companies Siminn had the largest market share which exceeded 80%.

35. The PTA considered that competition on the market in question was severely limited by entry barriers. The main factors mentioned in this respect were infrastructure that was difficult to duplicate and a high risk of sunk costs for new companies.

36. The PTA also considered that economies of scale and scope could also discourage other companies from commencing operations and in addition to this that technology on the market was relatively mature and did not offer opportunities for advancement that could arouse the interest of new companies.

37. The Siminn bundling in electronic communications services for fixed line telephony, mobile and data transfer services was considered to strengthen the company's position on the relevant market. Both vertical and horizontal integration in Siminn operations constituted market dominance in the opinion of the PTA. This was considered to be found in the transfer of market power from wholesale to retail level without mitigating measures in the form of obligations at wholesale level.

38. In addition to this the PTA reached the conclusion that purchasers faced limited choice of service provider and that countervailing buying power on the market was not adequate to influence sellers' market power. In addition to this the PTA consider there to be little likelihood that purchasers would install their own lines to fulfil their electronic communications needs. Purchasers of leased lines at retail level were mainly companies, associations and public institutions that use them to connect their offices and operational centres at various locations around the country.

39. The PTA considered that Siminn enjoyed a dominant position on the market and that active competition would not flourish during the estimated period of validity of the analysis, inter alia because there was little likelihood that purchasers would install their own lines to fulfil their telecommunications needs.

40. Subsequent to the analysis, Siminn was designated as having significant market power and obligations were imposed on the company for the purpose of achieving the objectives of electronic communications legislation for competition on the relevant market. The obligations imposed on Siminn were as follows:

- The obligation to offer specific types of lines for lease
- Non-discrimination
- Transparency
- Accounting separation
- Price control (cost analysis based on historical costs)

5.0 The position on the market in question

41. When the prior analysis was made by the PTA, Siminn enjoyed a dominant position on the retail market for minimum set of leased lines, a market share in excess of 80%, and thus other companies all with considerably less. Although Siminn is still by far the largest on the market, the scope of the market and its significance have however diminished to such an extent as a result of technical developments that one must take this particularly into account in the analysis.

42. The transmission capacity used in the market today is far greater than what the definition of the minimum set allows for, i.e. up to and including 2Mb/s. Most widely used replacement is 12Mb/s xDSL connections, which the PTA considers under the M5 market definition. The remedies imposed on the wholesale market for terminating segments of leased lines provide for equal access to and transparently priced products that fuel a competitive retail market for leased lines for those end-users that have needs the xDSL solutions do not fulfil. PTA has found it unnecessary to extend the retail market for a minimum set of leased lines in light of the status of this competition.

43. The development of new technology has meant that the significance of the market has significantly diminished in recent years. This means there is no longer much latitude for electronic communications companies to operate on the relevant market. The market consists of legacy products that are in the sunset period of their lifecycle. New entrants are not interested in offering end-users these products and technologies, since they have newer and more economic solutions available.

44. Today most companies prefer to use a variety of high speed data transfer solutions such as IP and ethernet protocols over copper and fibre-optic transmission infrastructure. Those companies that still use connections slower than 2 Mb/s mainly use them to connect two operational premises that are geographically distant from each other but such parties are steadily decreasing.

45. Only two companies, Siminn and Vodafone, operate on the relevant market to any significant degree. In 2012 Siminn was by far the largest on the market with about [90-95%]¹² market share by revenue while Vodafone had about [5-10%].¹³

46. The above specified companies that operate on the retail market also operate on related wholesale markets¹⁴ such as termination of leased lines (M6) and the bit stream market (M5), which enables them to offer a variety of high-speed solutions. Wholesale remedies that are in effect on markets 5 and 6 are establishing effective competition in the downstream retail market.

47. In the year 2011 Siminn's external revenue from retail sale of leased lines slower than 2 Mb/s totalled approximately ISK [...] million.¹⁵ The reduction in revenue since 2005 has been significant because in 2005 Siminn revenue, adjusted to 2012 average prices, was

¹² Margins for confidentiality.

¹³ Margins for confidentiality.

¹⁴ In the case of Siminn its sister company Mila also has wholesale operations.

¹⁵ Removed for reasons of confidentiality.

approximately ISK [...] ¹⁶ million. The real reduction is thus close to 80% for this period (see figure 5.1).

Figure 5.1 Siminn revenue for the period 2005-2012 adjusted to prices for 2012

[...] ¹⁷

48. Total revenue from data transmission (IP-VPN, broadband connections, leased lines etc.) was approximately ISK 4.8 billion in Iceland in the year 2012. Total revenue of leased lines that belong to the relevant retail market was at the same time approximately [...] ¹⁸ of total revenue. This shows that the significance of the relevant market has diminished greatly.

49. The status of the retail market for minimum set of leased lines is in the opinion of the PTA such that technical innovation and alternative products have to a large extent replaced the products that belong to the market. The scope of operations on the market has diminished steadily in recent years and is now only a quarter of what it was during the period of the 1st analysis and developments all tend towards diminishing scope. This demonstrates that users choose rather leased lines with greater capacity or other data transmission solutions than leased lines with a maximum of 2 Mb/s.

¹⁶ Removed for reasons of confidentiality.

¹⁷ Removed for reasons of confidentiality.

¹⁸ Removed for reasons of confidentiality.

6.0 Evaluation of conditions for imposing obligations on the relevant market

6.1 General

50. According to Articles 16 and 17 of the Electronic Communications Act the definition and analysis of markets shall be made in accordance with obligations according to the EEA Agreement. In the Regulation on Market Analysis in the field of Electronic Communications no. 741/2009, the methodology is introduced that is described in the ESA Recommendation on the relevant market and in the ESA Guidelines for market analysis. In the Regulation one can find a listing of the markets specified by ESA in its Recommendation and in Article 4 of the Regulation there is discussion on the conditions that markets need to fulfil in order to be susceptible to obligations pursuant to Chapter VII of the Electronic Communications Act no. 81/2003.

51. The retail market for minimum set of leased lines (Market 7 in the prior ESA Recommendation) has been removed from the list in the ESA Recommendation for the markets that are pre-designated as lacking competition. Despite the fact that the market is no longer in the ESA Recommendation, this does not automatically mean that possibilities for administrative intervention do not exist in Iceland. The market needs to be re-examined as the PTA has designated undertaking with significant market power on this market and it has to be decided whether this designation should be maintained or whether it should be withdrawn. Circumstances may be such in this country that the market fulfils the requirements for susceptibility to ex ante obligations, though in general terms, this may not have been considered to apply in EEA states when the Recommendation was reviewed. In Items 21 and 22 of the Preamble to the ESA Recommendation from 2008 there was discussion on instances where regulatory authorities may have reason to deviate from the Recommendation. There it is stated, among other things, that if a market that was in the Recommendation from 2004 is not in the new Recommendation, the electronic communications regulatory authorities can examine whether it still fulfils the conditions for ex-ante obligations given the circumstances of the country in question.

52. This means that if the PTA considers that circumstances are such in this country that the position on some of those markets that have been removed from the Recommendation differs from the norm in the EEA area, such that barriers to entry are still high, competition not foreseeable in the near future and general competition rules do not suffice to resolve market problems, then the PTA can request endorsement from ESA to examine the relevant market with a view to making a decision on obligations. The PTA can provide as a single submission to the ESA an evaluation of whether the market fulfils the three criteria¹⁹, an analysis of the market and a description of planned obligations.

53. In evaluating whether the market still fulfils the conditions to be susceptible to ex-ante obligations on companies on the market²⁰, the same methodology shall be used as when the market was specified in the Recommendation. The three criteria that the relevant market

¹⁹ The Three Criteria Test. Three criteria test).

²⁰ See Articles 6, 7 and 15 of the Framework Directive, Items 6 and 22 of the preamble to the ESA Recommendation on the relevant market from 2008, Chapters 2.2 and 2.3 in the Explanatory Note to the Recommendation of the EU on the relevant market from 2007.

needs to fulfil are the following:²¹

- 1) That there exist high and non-transitory barriers to entry, whether they result from organisational, legal or administrative causes. It should be taken into consideration whether it is possible to surmount such barriers during the period of reference, taking into account the flexibility of electronic communications markets.
 - a. Entry barriers related to organisation and structure of the market can for example be related to the scope of an electronic communications network, sunk costs and control of infrastructure that are difficult to duplicate.
 - b. Legal and administrative barriers can for example be related to the allocation of frequency ranges.
- 2) That active competition cannot be foreseen during the reference period. In connection with this, one must among other things examine the competition conditions that pertain within the entry barriers.
- 3) That the application of existing Competition Law would not on its own suffice to provide remedies where the market has failed. The following conditions could indicate that the above:
 - a. If major action is required to redress a failure by the market.
 - b. If intervention is required relatively often and without delay.
 - c. If special action is required to create legal predictability.

The market needs to fulfil all the above criteria in order for it to be possible to impose obligations pursuant to Articles 27-32 of the Electronic Communications Act.

54. The following is an examination by the PTA on whether these conditions apply to the retail market for minimum set of leased lines in the light of the circumstances in this country. It will be examined whether the above specified ESA Recommendation apply to Icelandic circumstances, taking into consideration market circumstances in this country as they are now in the relevant market.

55. In the Explanatory Note to the EU Recommendation from 2007²² it is stated that if appropriate obligations are imposed on an undertaking with significant market power, where appropriate, it is not likely that consumers will suffer on the retail market for minimum set of leased lines. Wholesale obligations, where appropriate, should thus suffice to ensure adequate competition and supply on the retail market. In the Explanatory Note it is also stated that as the appropriate regulatory framework is in place on the wholesale market then few barriers to entry should exist. Companies thus have the option of offering a variety of leased line services to end users. The EU Commission has proposed that there be no minimum set of leased lines

²¹ ERG has issued a document where these conditions are discussed in more detail; ERG Report on Guidance on the Application of the Three Criteria Test - ERG (08) 21 ERG Report on 3 criteria test final 080604.

²² Explanatory Note. Accompanying document to the Commission Recommendation on Relevant Product and Service Markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services (Second edition) {(C(2007) 5406)}, bls. 39.

in retail.²³ In accordance with the conclusions of the EU Commission this market was removed from the ESA Recommendation when the authority issued a new Recommendation for the relevant market on 5 November 2008.

Despite the fact that this market is no longer part of the ESA Recommendation it is necessary to re-examine the market as there are currently obligations in force on this market that were imposed by the PTA with its Decision dated 14 September 2007. It has to be established whether the circumstances are currently such in this country that it is justifiable to intervene in this market and a decision has to be made on whether the obligations should remain in force unchanged or changed, or whether they should be withdrawn. The following is the PTA assessment of whether the market still fulfils the relevant conditions.

6.2 First criterion: High and non-transitory barriers to entry

6.2.1 General comments on barriers to entry

56. The first criterion that needs to be fulfilled for there to be a reason to intervene in a market with ex-ante obligations according to the Electronic Communications Act is that there are high and non-transitory barriers to entry to the relevant market.

57. 'Entry barrier' is a collective term for various factors that can influence companies' market power. If there are few barriers to a market then possible profitability is an attraction for new companies to gain market share from incumbents. Possible competition from new parties can influence the behaviour of a company with SMP and can diminish its harmful influence on competition. Entry barriers on the other hand weaken or prevent competition.

58. Here in this country there are no significant legal barriers to entry for new electronic communications companies. No special licences are needed to provide electronic communications services and all companies with their legal abode in the EEA or in member states of the World Trade Organisation are authorised to operate electronic communications services in this country, subsequent to a simple registration process. There is sufficient supply of leased lines in wholesale which means that this is not a limiting factor. There are no known instances where planning construction laws having created barriers with respect to location of equipment required by a retail seller of leased line services. In general, no legal barriers exist on this market.

59. In the analysis of Market 7 in 2007 the PTA examined a number of factors, with respect to whether entry barriers existed. The factors that were examined were as follows: control of infrastructure not easily duplicated, sunk costs, economies of scale and scope, access to capital, access to distribution and sales systems and barriers to growth. It was the conclusion of the PTA that there were significant entry barriers. But not all the factors that were examined were considered to constitute barriers. The PTA considered that access to distribution and sales systems and access to capital did not constitute entry barriers. The PTA also considered that technical changes could be a deciding factor as to whether control of infrastructure constituted an entry barrier. The Siminn economies of scale and scope were considered to constitute an entry barrier. The PTA considered that limited growth possibilities

²³ Explanatory Note. Accompanying document to the Commission Recommendation on Relevant Product and Service Markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services (Second edition) {(C(2007) 5406)}, bls. 39.

were a barrier to entry. Sunk costs were also considered to be a significant entry barrier but it was noted that this was not axiomatic and what mattered most in this respect was the small size of the market and the price of leased lines.

60. In the following sections there will be discussion on the issues examined by the PTA with respect to entry barriers in its analysis from 2007 and an assessment will be made of the impact they have on the market today.

6.2.2 Control of infrastructure not easily duplicated

61. If a company has control of infrastructure that is expensive to duplicate, then this can represent a significant barrier for potential competitors.

62. In its analysis of Market 7 in the year 2007, infrastructure not easily duplicated was considered to be a significant entry barrier. The Siminn electronic communications network continued to be so large that it was not realistic to expect that other companies could develop analogous infrastructure. Though this might be academically possible the costs and the time required would have been such that it was out of the question.

63. The PTA designated Siminn and Mila as having significant market power on the wholesale market for leased lines in 2007 and imposed obligations that assured access to any kind of leased line in wholesale at reasonable terms. Siminn has now discontinued operations on the wholesale market for leased lines while its sister company Mila sells all kinds of leased lines in wholesale in accordance with obligations in force. In the preliminary draft to the market analysis for the wholesale market for the terminating segments of leased lines (market 6) it is prescribed that wholesale obligations be maintained on Mila. Because of these obligations, operators do not need their own network system to be able to compete on the retail market. Having one's own network system is no longer a prerequisite for entry to the market.

64. With the changes in mind that have taken place on Market 7 and the obligations that have been imposed on the related wholesale market, the PTA considers that control of infrastructure not easily duplicated is not a significant entry barrier.

6.2.3 Sunk costs

65. When a company enters a new market it needs to perform certain preparatory work and to invest in specific start-up costs. If entry to a market fails it can sometimes be possible to recover such costs, for example with the sale of basic investments and equipment. Sunk costs are those costs that the new entrant has to bear as a loss should he fail to establish himself on the market. Sunk costs are a barrier to entry, because the incumbent companies on the market do not have to bear them. Their costs in most instances have already been paid.

66. The PTA concluded in 2007 that it was not axiomatic that large sunk costs had to be incurred in order to be able to offer leased lines at retail level when a wholesale market existed. That price and the small size of the market did not give reason to believe that it would be profitable to operate solely as a resale party for leased lines on the retail market. The PTA considered that companies that intended to offer leased lines to any degree on the retail market needed to own at least some part of the necessary equipment. The PTA pointed out that the substantial Siminn investment in leased lines had a long history and that Siminn had built up strong customer goodwill throughout the years while other possible competitors

would be more dependent on the start-up costs of new investments.

67. The PTA considers that access today to wholesale leased lines is better than it was in 2007. There is a great variety of offers of lines at cost oriented prices and a comprehensive reference offer is published where all potential retail parties can acquaint themselves with the service offer and terms. Because of the small size of the retail market it is not realistic to embark on major investments and nor is it likely that a company would be launched for the purpose of offering leased lines solely at retail level. On the other hand the retail of leased lines can be an important addition to the service of an electronic communications company that wishes to offer comprehensive service on the electronic communications market. To meet this need there is, in the opinion of the PTA, an adequate offer of leased lines at wholesale level and at acceptable terms. For this reason there is no need to invest significant sunk costs in order to be able to enter the retail market. The PTA therefore considers that sunk costs are no longer a significant entry barrier.

6.2.4 Economies of scale and scope

68. Economy of scale exists in the operations of companies when increased production results in lower total costs per unit. This is characteristic of technical companies which have relatively high fixed costs and low variable costs. Economy of scale can work both as an entry barrier for new parties and as an advantage over other competitors.

69. Parties operating on the retail market can now purchase lines at cost oriented prices that are based on costs in Mila's leased line operations. They are offered the same price as Siminn as a result of the non-discrimination obligation on wholesale markets for leased lines which was imposed in 2007. For this reason the unit price to parties on the retail market is the same regardless of their size and turnover. Economy of scale can however result from the operation of related systems such as sales and service systems and transfer routes. The PTA considers that economies of scale and scope are no longer a significant entry barrier to the relevant market as all parties are offered the purchase of the underlying wholesale service at the same price.

6.2.5 Access to capital

70. Access to capital can have a deciding influence on the possibilities for a company on a competitive market. This particularly applies to markets that demand high initial investment. The difference between companies, with respect to access to capital could be a barrier to entry. Financially strong companies with good access to capital, other things being equal, are in a better position and can more easily protect themselves from competition than comparable companies that do not have as good access to capital. Good access to capital can both represent an entry barrier and can indicate market power.

71. In the prior analysis from 2007 the PTA concluded that access to capital did not create an entry barrier to the relevant market. Taking into account circumstances on the market today and the fact that obligations on the wholesale market have reduced the price of entry to the market for companies, the PTA still believes that access to capital is not an entry barrier to the relevant market.

6.2.6 Access to distribution and service systems

72. Well-developed service systems can act as an entry barrier for new parties and as a

competitive advantage. This particularly applies on markets where substantial costs are tied up in the development of distribution and sales systems or where all the companies have made sole agreements with the largest and/or most important distribution parties on the market.

73. In its prior analysis the PTA came to the conclusion that access to distribution and sales systems was not an entry barrier to this market. The reason for this was that purchasers on the market are usually specialised companies that base their procurement on tenders. The PTA still considers that circumstances on the market are such that access to distribution and sales systems is not an entry barrier to the relevant market.

6.2.7 Barriers to expansion

74. A market with significant potential for growth is much more attractive to new operators than a stagnant (mature) market. It is probable that undertakings contemplating entry into a stagnant market must lure customers away from established operators. If there are limits to a market's potential to grow and offer more extensive services, entry barriers may exist.

75. In the previous analysis from 2007 the PTA concluded that the market for a minimum set of leased lines was mature and it was not expected that the number of channels or revenue would increase in the near future. It was also pointed out that many users had started to connect to the Internet through other services such as with xDSL service.

76. The PTA considers that the market is still mature and that there are few opportunities for growth. The market has shrunk somewhat since 2007 and for this reason it is clear that development tends towards a steady reduction in growth opportunities. Many users would rather use DSL standards on copper local loops or GPON/P2P standards on fibre-optic local loops. For this reason there is not so much to compete on and the significance of the market has significantly diminished. The PTA considers that barriers to growth to exist and that they are a barrier to entry.

6.2.8 Conclusion with respect to entry barriers

77. From the above discussion one can see that the most significant entry barriers that once existed on this market are no longer in place to the extent that they can be described as high and non-transitory. The only entry barrier that the PTA considers to exist today is the shrinking of the market. The PTA considers that those companies that need to offer their customers retail leased lines have easy access to wholesale service which serves their needs because of the obligations were imposed on Mila on the wholesale market for leased lines in 2007. The PTA has not observed any new entry barriers to the markets. The PTA therefore considers that the market does not fulfil the first criterion that must be in place if the implementation of obligations is to be an option.

78. As all three criteria discussed in Chapter 6.1 need to be fulfilled in order to be able to apply obligations, and as the relevant market no longer fulfils the first criterion in the opinion of the PTA, it is not necessary to examine criteria numbers 2 and 3, with respect to development towards active competition and to the application of general Competition Law. It is furthermore unnecessary to perform additional analysis of the competitive position on the market.

79. As stated previously it was noted in the European Commission Explanatory Note to the Recommendation on the relevant market from 2007 that in those locations where the wholesale market connected to the relevant retail market had been analysed and obligations imposed, as appropriate, this had sufficed for competition to become active on the market for a minimum set of leased lines. The fact that this is the situation in Iceland supports the PTA conclusion that the imposition of obligations is not an option under consideration on the retail market for the minimum set of leased lines (previously Market 7) in this country under current circumstances.

80. The PTA nevertheless considers there to be a need to continue to closely monitor the market and is prepared to examine whether a new analysis needs to be made should circumstances on the market change significantly.

7.0 Withdrawal of obligations

7.1 General

81. As the conclusion of the PTA, after assessing circumstances on the relevant market is that there are no longer high and non-transitory entry barriers to the market then the conditions are no longer in place for imposition of ex-ante obligations on undertakings on the market according to the Electronic Communications Act or that undertakings be designated as having significant market power. The next step is clearly to withdraw the designation of Siminn as an undertaking with significant market power and those obligations that were imposed on Siminn on this market.

7.2 Obligations currently in force

82. With the PTA Decision no. 20/2007 dated 14 September 2007 the following obligations were imposed on Siminn as an undertaking with significant market power on the market that was then Market 7.

a) Obligation for access to retail leased lines

83. The obligation is imposed on Siminn to provide access to those leased lines itemised in the definition of minimum set. Such access should be on offer across the whole country. In addition to this Siminn was to ensure that the service that was on offer on the publication of the decision should remain on offer for a reasonable duration and that it was only authorised to cancel the service in collaboration with the users in question and with prior endorsement from the PTA.

b) Obligation for non-discrimination

84. The obligation was imposed on Siminn to practise non-discrimination when selling leased lines on the retail market. Siminn was to provide all purchasers of leased lines with service with analogous terms, prices and quality. Siminn was to organise its operations in such a manner that Siminn maintain confidentiality on information gained with the sale of leased lines. It was unauthorised to provide other parties with information on transactions with other companies with respect to potential purchase, including other departments in Siminn, subsidiaries and partners, see Article 26 of the Electronic Communications Act.

c) Obligation for transparency

85. The obligation was imposed on Siminn for transparency and that Siminn should prepare and publish information on the following issues with respect to retail leased lines:

Tariff

Technical characteristics and basic requirement limitations

Conditions for delivery and use

Connection of user equipment

Delivery terms, inter alia:

- Information regarding method of ordering;
- Delivery notice, which would be counted from the day that the user

presented a formal request for a leased line until the time when 95% of all leased lines of the type in question had been installed with users;

- Duration of agreement, i.e. the period of time defined in the agreement and the minimum agreement duration that the user was obliged to agree to;
- Repair time which is the period of time from the time that a notification of fault had been received by the company in question until the time when 80% of all leased lines of the same type had been repaired. If an offer is made for repairs in varying quality categories for the same types of leased lines, information should be published on a variety of typical repair times;
- Rules on repayment.

d) Obligation for accounting separation

86. The obligation was imposed on Siminn to distinguish between wholesale on the one hand and retail on the other. Siminn should provide the PTA on an annual basis with a breakdown of the operational accounts and balance sheet for wholesale and retail along with a statement of the division of indirect costs that were not possible to allocate through comparison with other cost items. Then Siminn was to enter its bookkeeping in such a way that it would be possible to allocate all revenue and costs in operational accounts to various services.

87. Siminn was furthermore to provide the PTA on an annual basis with an opinion on the execution of accounting separation. The opinion was to be provided by independent parties who have knowledge and skills in the relevant fields. The following, as a minimum, was to be shown in the opinion:

- The conclusions of the party that conducted the audit.
- Statement of all instances of inconsistency.
- Proposals by the party conducting the audit for remedies and their impact.
- Detailed description of how the audit was performed.
- Consolidated financial and bookkeeping information (for example an opinion with respect to the distribution of common costs and changes to assessment of assets to value in use).

e) Obligation for price control

88. The PTA imposed the obligation on Siminn for price control for the minimum set of leased lines. Siminn was to make a cost model for calculation according to historical costs. The cost model was to be completed within one year. Siminn was also required to introduce cost accounting that captured, identified, assessed and allocated the relevant costs to the services or products in accordance with recognised rules. Siminn was also to deliver to the PTA a description of the cost accounting and to publish the main cost categories and rules that were used to allocate costs. Then Siminn was to notify all changes to the PTA and they would not come into force without prior endorsement of the PTA.

7.3 The impact of existing obligations

89. Obligations on the minimum set of leased lines ensured that there was a sufficient offer of leased lines to end-users at reasonable rates. This particularly applied to the statutory obligations that were in place prior to the market analysis of 2007. After the obligations on wholesale markets for leased lines began to have an effect there was not the same need for obligations on the retail market because now all electronic communications companies could offer retail leased lines. The impact of obligations on the retail market has diminished since the year 2007.

90. The very substantial shrinkage of the market for low speed lines that are included in the defined minimum set, further limits the importance of obligations at retail level.

7.4 Planned Decision and its coming into force

91. As was previously stated, the PTA plans to make a Decision subsequent to this analysis to the effect that the designation of Siminn as an undertaking with significant market power on market for the minimum set of leased lines (previously Market 7) be withdrawn.

92. In Paragraph 3 of Article 16 of the Framework Directive, 2002/21/EC, and in the Explanatory Note to the EU Recommendation from 2007²⁴ it is stated that when obligations are withdrawn, those parties that are affected by the decision are given an adequate glide path to adapt. The same kind of provision can be found in Paragraph 6 of Article 9 of the Regulation on Market Analysis no. 741/2009, where it is stated: *Should the Post and Telecom Administration decide to withdraw obligations that have been in force, then this shall be notified to the parties affected by the decision with adequate notice before the decision in question is implemented.* The PTA considers it appropriate and proper to follow this rule.

93. Those parties first and foremost affected by the decision to withdraw obligations are those companies that have transactions with Siminn on the basis of obligations in force. The withdrawal of obligations can also have an indirect effect on other parties on the market or that are related to the market.

94. It is the PTA's conclusion that the relevant retail market is no longer characterised by high and non-transitory barriers to entry and this market thus does not fulfil all the necessary conditions for the imposition of ex-ante obligations.

95. In addition to this the PTA points out that obligation on the wholesale markets for leased lines should in the opinion of the EU Commission suffice on their own to establish effective competition on the relevant market.

96. The PTA considers that those companies that need to offer their customers retail leased lines have easy access to wholesale service which serves their needs because of the prevailing obligation on Mila on M6. The wholesale prices which apply to Mila on M6 today will be in effect until the PTA has endorsed the new cost analysis of Mila. It is the opinion of PTA that the said wholesale prices are not a problem on the market today and will not be for the next several months.

97. The scope of this market has also, due to technical developments, diminished

²⁴ See page 50 in the notes.

dramatically. Therefore, the significance of this market has significantly diminished in recent years. Today, most companies prefer to use a variety of high speed data transfer solutions, such as IP and ethernet protocols over copper and fibre-optic transmission infrastructure.

98. The withdrawal of obligations could result in the need to review agreements in force to some extent, or to make new agreements. Some customers could need or wish to switch service providers on the retail market because of changed circumstances. It is not certain that any of these actions may need to be taken but if this is the case to some extent, there could be a need for a period of adaptation.

99. The PTA considers it most important that access is assured over a period that should suffice for adaptation. The PTA considers that as it is possible to approach more than one party for resale of leased lines and because switching service providers for individual leased lines does not require much preparation, the period does not need to be particularly long. The PTA therefore intends to prescribe that obligations on Siminn on the relevant market be withdrawn after 3 months from the publication of the Decision following this analysis.

100. The PTA points out that the Administration did not receive any comments from stakeholders in the national consultation in the 2 months period that the consultation lasted on the withdrawal of Siminn's SMP designation and the following withdrawal of obligations.