

Brussels, 6 December 2012
Case No: 72796
Event No: 654378

Póst-Og Fjaraskiptastofnun (PTA)
Sudurlandsbraut 4
108 Reykjavik, Iceland

For the attention of:
Mr Hrafnkell V. Gíslason
Managing Director

Dear Sir,

Subject: Wholesale market for call origination on the public telephone network provided at a fixed location in Iceland

Wholesale market for call termination on individual public telephone networks provided at a fixed location in Iceland

Wholesale market for transit services in the fixed public telephone network in Iceland

Comments pursuant to Article 7(3) of Directive 2002/21/EC (Framework Directive)¹

I. Procedure

On 6 November 2012, the EFTA Surveillance Authority (the “Authority”) registered three notifications from the Icelandic national regulatory authority, *Póst-Og Fjaraskiptastofnun* (the “PTA”), concerning draft measures on (i) the wholesale market for call origination on the public telephone network provided at a fixed location in Iceland;² (ii) the wholesale market for call termination on individual public telephone networks provided at a fixed location in Iceland;³ and (iii) the wholesale market for transit services in the fixed public telephone network in Iceland.⁴

¹ 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, OJ L 108, 24.4.2002, p. 33 (as amended by Regulation (EC) No 717/2007, OJ L 171, 29.6.2007, p. 32 and Regulation (EC) No 544/2009, OJ L 167, 29.6.2009, p. 12), as referred to at point 5cl of Annex XI to the EEA Agreement and as adapted to the Agreement by Protocol 1 (the “Framework Directive”).

² Corresponding to market 2 in 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 Framework Directive, adopted by Decision No 688/08/COL, OJ C 156, 9.7.2009, p.18 (the “Recommendation on relevant markets”).

³ Corresponding to market 3 in the Recommendation on relevant markets.

⁴ Corresponding to market 10 in the EFTA Surveillance Authority Recommendation (No 194/04/COL) of 14 July 2004 on relevant product and service markets within the electronic communications sector susceptible to *ex ante* regulation in accordance with the Framework Directive, as incorporated into the Agreement on the

The notifications became effective on the same day. National consultation pursuant to Article 6 of the Framework Directive was carried out in the period from 26 June 2012 to 21 August 2012.

The period for consultation with the Authority under Article 7 of the Framework Directive expires on 6 December 2012.

Pursuant to Article 7(3) of the Framework Directive, national regulatory authorities (“NRAs”) and the Authority may make comments on notified draft measures to the NRA concerned.

II. Description of the draft measures

II.1. Previous notifications

The first review of the wholesale markets for call origination, call termination and transit services on the fixed public telephone network in Iceland was notified to and assessed by the Authority in 2008.⁵

Following that review, Síminn hf. (“Síminn”) was designated as a provider with significant market power on all three markets and Fjarskipti ehf. (“Vodafone”) on the market for call termination services. Specific obligations were imposed on all operators.⁶ The Authority, *inter alia*, invited PTA to inform it of the progress made on the cost accounting obligation imposed and to notify any amendments to this obligation to the Authority.

II.2. Market definition

The relevant product and geographic markets are defined as follows:⁷

II.2.1. The wholesale market for call origination on the public telephone network provided at a fixed location: the service considered to be part of this market is the origination of calls, choice of route in the telephone exchange and connection for the origination stage of the call. Transit from the end user by local copper loop to the distribution frame and from there to the first telephone exchange on the route before reaching the next stage is included, the next stage being either transit or termination of the call. The relevant market also comprises call origination for the purpose of accessing dial-up Internet service provision. Calls between networks or entirely within the same network belong to this market. PTA considers the geographic market for call origination to be national in scope.

II.2.2. The wholesale market for call termination on individual public telephone networks provided at a fixed location comprises the termination of a call and the choice of route at

European Economic Area (the “2004 Recommendation”). The wholesale market for transit services in the fixed public telephone network is no longer included in the Recommendation on relevant markets.

⁵ See the Authority’s “comments letter” of 1 December 2008 (Event No 499523).

⁶ Síminn was obliged (*inter alia*) to offer the relevant services at cost-oriented prices. It was also required to prepare a cost model for price calculation using historical costs as a reference within six months of the publication of PTA’s decision. PTA envisaged – based on the results of the cost analysis and on comparison with prices in other EEA States – to assess whether it would be more suitable to use the long-run incremental cost (“LRIC”) method rather than the historical costs of Síminn. Vodafone was obliged to offer call termination prices on the basis of a four-year glide path eventually resulting in symmetrical prices with those of Síminn.

⁷ PTA notes that the market definitions in the current draft measures are the same as in PTA’s first round of analyses of the relevant markets in 2008.

the termination end of a call. Termination constitutes transit of a call from the preceding stage in the route of the call (origination or transit) through a telephone exchange and by way of local copper loop to the party being called. Calls between networks or entirely within the same network belong to this market. PTA considers the geographic market for call termination to be national in scope.

II.2.3. The wholesale market for transit services in the fixed public telephone network in Iceland is defined as the transit of telephone traffic through at least one exchange (for example tandem switch/media gateway) which is not the exchange closest to final users in a telephone call. PTA considers that, given the circumstances in Iceland where the whole country is one interconnection area, transit of calls only takes place where a call goes from one network through a fixed line network to a third network. PTA considers that the relevant geographic market is national in scope.⁸

In its conclusion regarding the relevant markets, PTA explicitly includes in the scope of the relevant markets the various service elements necessary for network interconnection and offered at the wholesale level in relation to origination, termination and transit services.

II.3 Finding of significant market power (“SMP”)

II.3.1. Wholesale market for call origination on the public telephone network provided at a fixed location in Iceland

PTA designates Síminn as individually possessing SMP on the basis of, in particular, Síminn’s high market share of approximately 60% based on traffic volumes,⁹ Síminn’s overall size and experience in the electronic communications market, considerable entry barriers, economies of scale and scope, Síminn’s highly developed distribution and sales network, barriers to growth, vertical integration, limited countervailing buying power, limited potential competition and shortage of freedom of choice as well as high switching costs.

II.3.2. Wholesale market for call termination on individual public telephone networks provided at a fixed location in Iceland

On the basis of its market analysis, PTA concludes that the following operators individually possess SMP within their networks providing call termination at a fixed location: Síminn, Vodafone, Nova ehf. (“Nova”), Símafélagið ehf. (“Símafélagið”) and Hringdu ehf. (“Hringdu”) have 100% market shares in their own fixed-line networks. The criteria relied upon by PTA in its determination of the SMP are, for all operators, *inter alia*, a 100% market share, price developments and limited countervailing buying power.

⁸ PTA considers that the definition of geographical markets used in the market analysis in 2008 still applies. The country is still one interconnection area and not divided into smaller areas. Changes that have taken place on the market do not warrant, in PTA’s opinion, a division of the country into smaller areas as the fixed line telephone network of Síminn covers the whole country and that of Vodafone has extensive coverage (although some companies have smaller networks that are only operated in the capital city area of Reykjavik). In addition, no distinction is made between different regions with regard to tariffs. The same laws and regulations apply to the operation of fixed line telephone networks everywhere in Iceland and a company’s licence to operate a network applies throughout the country. It is not possible to demarcate areas in the country where conditions for competition are significantly different from those which apply in other areas.

⁹ In 2011, Síminn’s market shares in terms of total revenues from domestic fixed line telephone services were between 65-70% and 60% in terms of the total number of minutes. Vodafone’s market share was 38%. Other operators had around 2% market share.

II.3.3. Application of the “three-criteria” test on the wholesale market for transit services in the fixed public telephone network in Iceland¹⁰

PTA assesses whether the market for transit services on the fixed public telephone network in Iceland remains susceptible to sector-specific *ex ante* regulation on the basis of the application of the “three-criteria” test.¹¹

Under the first criterion, PTA concludes that the transit market as a whole is no longer characterised by high and non-transitory barriers to entry. The main reason for this view is the fact that there has been a significant increase in the number of interconnections of networks since 2008, when only Síminn was considered to enjoy market power on the transit market.¹² At present, all operators which require transit can choose other routes than through Síminn’s network as there are seven companies operating fixed line and mobile phone telephone services that can offer transit services to a certain degree. Due to the network topology in Iceland, PTA considers that, in any event, there is no need for extensive networks to handle call transit and that it is sufficient to have a telephone exchange and interconnection with at least two networks. Furthermore, according to PTA, the cost of duplicating the facilities required for call transit has become manageable for new operators due to the introduction of cheaper technologies on the market.

In addition, an increasing number of providers have entered into direct interconnection agreements between each other¹³, which means that they have an alternative to Síminn’s offer of third-party transit and that they can offer third-party transit without significant extra investment. PTA also notes that these developments have taken place despite the transit market being a relatively marginal market with falling volumes, i.e. with the supply of transit services exceeding demand.

In PTA’s view, there are also no current legal barriers in the relevant market.

Against this background, PTA also concludes that the second criterion is not met for the transit market and that there is therefore no need to assess the third criterion. As a result, PTA concludes that the market for transit services on the fixed public telephone network

¹⁰ The wholesale market for transit services on the fixed public telephone network is no longer included in the Recommendation on relevant markets. The reduction of the number of markets susceptible to *ex ante* regulation does not necessarily indicate that the markets removed from the previous list set out in the 2004 Recommendation are effectively competitive in each of the EFTA States and that *ex ante* regulation is no longer warranted. For markets not listed in the Recommendation on relevant markets, NRAs are required to apply the “three-criteria” test to the market concerned in order to assess whether, on the basis of national circumstances, a market is still susceptible to *ex ante* regulation.

¹¹ Under Article 2 of the Recommendation on relevant markets, this test requires that three cumulative conditions are met in order for markets not listed to continue to qualify for *ex ante* regulation: (i) the presence of high and non-transitory structural, legal or regulatory barriers to entry, (ii) a market structure which does not tend towards effective competition in the relevant time horizon, and (iii) the insufficiency of competition law alone to adequately address the market failure(s) concerned.

¹² In 2008, Síminn’s market share in terms of total transit traffic was 61%. At the end of 2011, Síminn’s share was about 60% and Vodafone’s 30%. The other service providers had a combined share of less than 10%. The basis for the assessment of these market shares was the traffic from the origination of calls in individual networks. However, the collection of reliable data on the transit market is difficult due to the fact that a significant part of transit takes place without any charges. Therefore, PTA assumes that – as Síminn still has by far the greatest share in the fixed line telephone network – it also has the largest share in the transit market.

¹³ This also leads PTA to the conclusion that the sunk costs and the economies of scale and scope in the transit market do not constitute an entry barrier.

in Iceland no longer qualifies for sector-specific *ex ante* regulation and considers that there is no basis for continuing to designate Síminn as an undertaking with SMP in that market.

II.4. Regulatory remedies

In the light of the above assessment of SMP, PTA intends to impose the following regulatory remedies.

II.4.1. In the wholesale market for call origination on the public telephone network provided at a fixed location, PTA proposes the following remedies to be imposed on Síminn:

- Access (including resale access in case of demand);
- Non-discrimination (both with respect to price and other factors, as well as towards external operations and between internal operations and external operations; the obligation for non-discrimination applies to interconnection and to resale access to the Síminn fixed line telephone system);
- Transparency and publication of a reference offer;
- Accounting separation;
- Price control.

As regards the setting of call origination fees,¹⁴ PTA considers that prices for origination should relate to costs incurred in an efficiently designed electronic communications network and be symmetrical. PTA considers the bottom-up LRIC model (either the LRIC, LRIC+, LRAIC or LRAIC+ model) appropriate for the calculation of origination prices.¹⁵

PTA plans to set origination prices on the basis of a benchmark¹⁶ based on the following criteria:

- Only EEA States where origination prices are calculated on the basis of a cost analysis which uses the BU-LRIC methodology and are available at the time when PTA undertakes the comparison exercise will be taken into consideration;¹⁷

¹⁴ Currently, Síminn's maximum prices for call origination and termination in fixed line networks are based on historical costs at the level of ISK 0.63 per minute and the connection price ISK 0.62 per call.

¹⁵ PTA considers that the "pure" LRIC method (Long-Run Incremental Cost, as envisaged for the calculation of termination prices) is not appropriate for the pricing of call origination. The main reason is that the network operator that provides wholesale services for call origination (such as carrier pre-selection or resale) would have no opportunity to collect a share in the business overhead costs related to the service in question. It can neither collect this from its termination service (using the "pure" LRIC approach) nor can it transfer costs to the user that calls, as the network operator has no business relationship with that user. It therefore has to be possible at the wholesale level for the network operator to recover the above specified share in costs from the service provider that uses his wholesale services. Therefore, PTA considers the BU-LRIC model, without the "pure" approach, to be most suited to calculating call origination prices in fixed line networks.

¹⁶ PTA considers benchmarking appropriate due to the high cost associated with implementing a current cost BU-LRIC model, which goes beyond the regulatory authority's limited budget.

¹⁷ In PTA's opinion, it is necessary to have a minimum of five comparison countries as the basis for a decision on price using benchmarking. PTA will publish the conclusions of the benchmarking exercise no later than 1 November each year (for prices that will apply as from 1 January the following year), subsequent to national consultation and consultation with the Authority. The first benchmarking exercise shall, however, be completed no later than 1 May 2013, or at the same time as the benchmarking exercise for

- Comparison shall be made with the price for single transit and with the price per minute of a three-minute call;
- Comparison shall be made using the average exchange rate in the relevant quarter;
- The resulting price shall not be higher than the arithmetical average in those countries that fulfil the above conditions during the period of reference.

Against this background, and in particular the imposition of benchmarking, PTA proposes to withdraw the cost accounting obligation currently imposed on Síminn on the market for call origination in public telephone networks provided at a fixed location.

II.4.2. In the wholesale market for call termination on individual public telephone networks provided at a fixed location, PTA intends to impose the following regulatory remedies on all providers of termination services:

- Access;
- Non-discrimination (both with respect to price and other factors, as well as towards external operations and between internal operations and external operations);
- Transparency;
- Accounting separation;
- Price control.

As regards price control, PTA intends to prescribe symmetrical termination rates on the basis of the following criteria, benchmarked¹⁸ against termination rates in countries that calculate their rates using a “pure” LRIC¹⁹ model:

- Only EEA States where termination rates are calculated on the basis of a cost analysis which uses the “pure” LRIC methodology and are available at the time when PTA undertakes the comparison exercise will be taken into consideration;²⁰

call termination is completed. The resulting prices will be in force as of 1 July 2013 and then set annually as of 1 January 2014.

¹⁸ PTA intends to use benchmarking on the basis of Article 12 of EFTA Surveillance Authority Recommendation of 13 April 2011 on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EFTA States, OJ C 340, 18.11.2012, p. 5 (the “Termination Rates Recommendation”), which foresees this possibility for NRAs with limited resources.

¹⁹ The pure LRIC model is the recommended approach under the Authority’s Termination Rates Recommendation.

²⁰ In PTA’s opinion it is not possible for termination rates to be calculated on the basis of the proposed benchmarking exercise on 1 January 2013 as none of the EEA States yet fulfill the above specified conditions for benchmarking. PTA expects, however, that in the near future these circumstances will change and it will be possible to carry out the benchmarking exercise. During the period of validity of the current proposed measure, PTA will regularly repeat the benchmarking exercise using the above criteria, and will decide the maximum call termination charge effective as from 1 January each year in accordance with the conclusions of the benchmarking. It will do so for the first time as of July 2013 and then annually as of 1 January 2014. PTA will publish the conclusions of the benchmarking exercise no later than 1 November each year (for prices that will apply as from 1 January the following year), subsequent to national consultation and consultation with the Authority. The first benchmarking exercise shall, however, be completed no later than 1 May 2013 and then annually as from 1 November 2013. Generally, all EEA States fulfilling the above criteria will be used for the benchmarking. However, PTA considers it necessary to have a minimum of five countries for comparison. Therefore, PTA states that the above timing is subject to there

- Comparison shall be made with the price for single transit and with the price per minute of a three-minute call;
- Comparison shall be made using the average exchange rate in the relevant quarter;
- The resulting price shall not be higher than the arithmetical average in those countries that fulfil the above conditions during the period of reference.

As regards the specific levels of termination rates, PTA intends to impose symmetry on all operators at the current level of Simmin's rates of ISK 0.63 per minute and ISK 0.62 per call as from 1 March 2013, until the benchmarking exercise has taken place.²¹ Vodafone's rates will be symmetrical with those of Simmin as of 4 December 2012.²²

Against this background and in particular the imposition of benchmarking, PTA proposed to withdraw the cost accounting obligation currently imposed on Síminn on the market for call termination in public telephone networks provided at a fixed location.

II.4.3. In the wholesale market for transit services in the fixed public telephone network, PTA proposes to remove the current obligations imposed on Síminn. These include the obligation to provide access, non-discrimination, transparency, price control and cost accounting.

PTA considers a transitory period of six months before the removal of the current obligations to be adequate in order to give the affected providers the possibility to adapt to a non-regulated transit market.

III. Comments

The Authority has examined the draft measures and has no comments.

IV. Final remarks

On a procedural note, the Authority recalls that any future amendments to, or more detailed implementation of, the draft measures consulted on in the current notifications will require re-notification in accordance with Article 7(3) of the Framework Directive.

Pursuant to Article 7(5) of the Framework Directive, PTA may adopt the resulting draft measures and, if it does so, shall communicate the final measures to the Authority.

The Authority's position on the current notifications is without prejudice to any position the Authority may take in respect of other notified draft national measures.

Pursuant to point 15 of the Procedural Recommendation, the Authority will publish this comments letter on its eCOM Online Notification Registry. The Authority does not consider the information contained in this letter to be confidential. However, you are

being at least five countries that meet the proposed conditions. Should this not be the case on 1 January 2013, the first benchmarking exercise will be postponed for at least six months, or until the number of countries meeting the conditions is sufficient.

²¹ PTA considers it appropriate to give the companies at least two months from the publication of PTA's final decision on the relevant market to adapt their retail prices to the decision.

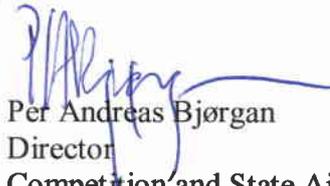
²² According to PTA's decision from 2008, Vodafone's rates should decrease in stages until they are symmetrical with Síminn rates. The last stage of the glide path shall enter into force on 4 December 2012, with the next change being introduced on the basis of the benchmarking exercise to be carried out by PTA.

invited to inform the Authority within three working days²³ following receipt of this letter if you consider, in accordance with EEA and national rules on confidentiality, that this letter contains confidential information which you would like to be deleted prior to publication. You should provide reasons for any such request.

Yours faithfully,



Ólafur Jóhannes Einarsson
Director
Internal Market Affairs Directorate



Per Andreas Bjørgan
Director
Competition and State Aid Directorate

²³ The request should be submitted through the eCOM Registry or by facsimile to +32 2 286 1800, marked for the attention of the eCOM Task Force.