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Comisión del Mercado de las
Telecomunicaciones (CMT)
Torre Mapfre
C/ Marina 16-18
08005 Barcelona
España

Attn: Mr. Reinaldo Rodriguez
Fax: +34 93 603 63 20
E-mail: chairperson@cmt.es
international@cmt.es

Dear Sir,

Subject: **Case ES/2005/0326: Publicly available local and/or national telephone services provided at a fixed location for residential customers**

Case ES/2005/0327: Publicly available international telephone services provided at a fixed location for residential customers

Case ES/2005/0328: Publicly available local and/or national telephone services provided at a fixed location for non-residential customers

Case ES/2005/0329: Publicly available international telephone services provided at a fixed location for non-residential customers

Comments pursuant to Article 7(3) of Directive 2002/21/EC¹

I. PROCEDURE

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 (the “Framework Directive”), OJ L 108, 24.4.2002, p. 33.

On 30 December 2005 the Commission registered a set of notifications by the Spanish national regulatory authority, the “Comisión del Mercado de las Telecomunicaciones” (“CMT”). The notifications cover the markets for publicly available international telephone services provided at a fixed location for non-residential and residential customers and publicly available local and/or national telephone services provided at a fixed location for non-residential and residential customers².

Pursuant to Article 6 of the Framework Directive³, a national consultation took place between 25 October 2005 and 25 November 2005. The deadline for the Community consultation under Article 7 of the Framework Directive is 30 January 2006.

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

II. DESCRIPTION OF THE DRAFT MEASURES

II.1 Market definition

The notifications concern the retail markets for publicly available international telephone services provided at a fixed location for non-residential and residential customers and publicly available local and/or national telephone services provided at a fixed location for non-residential and residential customers.

CMT considers that the markets include all telephony services through a fixed connection point over the public telephone network, either to fixed or mobile locations.

The following types of calls are considered as part of the relevant market:

- Local calls
- National calls
- Calls to mobile locations
- Calls to the Internet
- Calls to value-added services (automated reverse charges, shared payment, additional pricing, bulk calls or telephone polls)
- Calls to public and emergency services
- Calls to information services
- National and international operator-assisted calls

The markets therefore include telephony services through, in particular, a PSTN connection and an ISDN connection.

² Markets 3 to 6 in Commission Recommendation 2003/311/EC of 11 February 2003 on relevant product and services markets within the electronic communications sector susceptible to ex ante regulation in accordance with the Framework Directive (“The Recommendation”).

³ 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 (the “Framework Directive”), OJ L 108, 24.4.2002, p. 33.

CMT does not consider that IP-telephony services (VoIP) should be included in the relevant market since it considers that the VoIP service provided by Telefónica de Espana S.A.U. (“TESAU”) is complementary rather than a substitute to traditional PSTN telephony services because (i) since VoIP is broadband supported, the end-user has to maintain its PSTN line; (ii) from the end-user’s point-of-view, VoIP does not have the same functionalities as publicly available telephone services (provided over PSTN and/or ISDN); in particular it does not allow for complementary services such as access to emergency numbers or short numbers, pre-selection or selection of other operators, data services transfer, number portability, which are provided over the traditional PSTN telephony. The CMT does consider VoIP to be a source of potential competition.

International and national telephony services are regarded as separate markets. Based on the differences in demand characteristics and supply terms, CMT concludes that a distinction must be drawn between non-residential and residential customers in each market. The criterion for a customer to be described as a non-residential customer is that the customer has an organisation number (tax identification number) and residential customers are identified by a personal number.

In view of the above, CMT defines four markets for telephony services:

- publicly available local and/or national telephony services provided at a fixed location for residential customers;
- publicly available local and/or national telephony services provided at a fixed location for non-residential customers;
- publicly available international telephone services for residential customers
- publicly available international telephone services for non-residential customers

The relevant geographic market for the notified markets is the territory of Spain.

II.2 Finding of significant market power (“SMP”)

The CMT intends to designate TESAU as having SMP in all the relevant markets.⁴ The main criteria analysed by CMT when reaching its conclusion on SMP include: market shares; barriers to entry (legal barriers, sunk costs, economies of scale and scope, product differentiation); potential future competition from new services; control of infrastructure not easily duplicated; countervailing buyer power; switching costs; overall size of the undertakings; and vertical integration.

The analysis of market shares yields the following results for TESAU and its two biggest competitors in the respective markets:

Market – Operators	Market Shares (Revenues)		
	2003	2004	2005*

⁴ This designation encompasses TESAU as well as the group of companies to which TESAU belongs in its entirety.

Local / National - Residential			
TESAU	72,2%	69,5%	67,8%
Auna	10,9%	11,0%	10,7%
Grupo Ono	4,7%	5,0%	6,1%
International – Residential			
TESAU	67,6%	67,6%	68,4%
Auna	12,4%	10,7%	9,6%
Uni2	5,0%	4,2%	5,3%
Local / National – Non-Residential			
TESAU	79,0%	76,0%	77,3%
Auna	5,5%	6,0%	5,1%
Comunitel Global	3,2%	3,9%	4,0%
International – Non-Residential			
TESAU	63,7%	65,5%	67,9%
Uni2	13,8%	6,9%	11,0%
BT Espana	3,5%	7,3%	8,3%

*in June 2005

Based on the information contained in the table above as well as its analysis of the other structural and behavioural characteristics of the market, CMT concludes that TESAU has SMP in all of the defined markets.

II. 3 Regulatory remedies

The regulatory remedies that CMT envisages to impose on TESAU are aimed at addressing potential abusive practices such as inappropriate bundling; contractual and non-contractual market foreclosure; discriminatory pricing; as well as predatory pricing and margin squeeze.

The remedies intended to address these potential competition problems are transparency obligations defined as follows⁵:

- TESAU must communicate to CMT any changes to applicable prices and conditions of the relevant services at least 10 days before their effective date of application/launch date;
- TESAU must make available to CMT (within 10 days, on request) prices and conditions applicable to personalised offers offered by TESAU to those customers whose overall billing with TESAU exceeds €600,000 per year.

CMT proposes not to impose price control obligations, which it considers as unjustified and disproportionate. The main reasons for this are that it considers interconnection regulation at the wholesale level as sufficient to avoid anticompetitive behaviour by TESAU at the retail level.

⁵ Currently applicable regulation established in Decision PRE/4079/2005 consists of a price-cap mechanism and an ex ante communication obligation for retail tariffs for local, national and international calls, as well as fixed-to-mobile calls. Tariffs related to calls to directory enquiry numbers are submitted to an ex ante communication obligation (30 days). This Decision will cease to be applicable once the CMT has concluded its market review of the retail calls markets.

CMT does not impose strict accounting separation obligations either, such obligation being already imposed in the wholesale markets (market 8 and 9 of the Recommendation). CMT also considers that the risk of cross-subsidies as between retail services is not such as to warrant the imposition of a detailed accounting separation at that level.

III. COMMENTS

The Commission has examined the notification and the additional information provided by CMT, and has the following comment⁶:

Exclusion of IP-telephony in the notified markets: The Commission considers that the justification given by CMT for its decision to exclude IP-telephony from the notified markets is insufficient insofar as CMT's arguments are based on the fact that IP-telephony currently does not have the same functionalities as (and are thus not regulated like) publicly available telephone services (provided over PSTN and ISDN). When assessing whether or not IP-telephony should be included in any of the retail markets for fixed telephony services, the NRA should duly examine – taking account of national circumstances – the objective characteristics, prices and intended use of IP-telephony services, as well as their demand-side and supply-side substitution with other fixed telephony services. Such competition law-based, economic analysis is lacking from the notification.

The Commission notes that the broadband penetration rate in Spain is below EU average; and understands that there are currently only few VoIP offers on the market, which moreover can be distinguished from the retail telephony services covered by the notification in that they do not provide for guaranteed call quality and service levels. Also, the Commission notes that currently applicable wholesale regulation requires TESAU not to apply discriminatory conditions as between its own ADSL lines and its competitors' ADSL lines, and that by default, this wholesale obligation applies to VoIP⁷. Overall, the CMT's position that IP-telephony services have not yet had a considerable impact on the market is plausible. In any event, the Commission notes that the inclusion of IP-telephony in the notified markets, at this stage, would not have led to a different result as regards the SMP analysis.

The NRAs are called upon to make a prospective analysis of the relevant markets⁸. There are no reasons to exclude the possibility that VoIP may grow rapidly in Spain in the coming months as it has already done in other Member States, and that an array of new offers could be made available in the market that may be substitutable with the retail telephony services

⁶ Pursuant to Article 7(3) of the Framework Directive.

⁷ CMT Decision MTZ/2004/1950 regarding the modification of the use of the geographic numbers assigned to Telefónica de España S.A.U., 31 March 2005, page 10 (decision referred to on page 56 of the notification).

⁸ In this regard the Commission notes that in CMT's document "Conclusions on the public consultation on the provision of voice services using IP-based technologies (VoIP)" of 3 February 2005 (this document is referred to in the CMT Decision of 31 March 2005), page 4, CMT noted that "it could in principle be possible for CMT, as some operators have indicated, to carry out an analysis of the market and substitutability, which may result in the identification of new markets relating to VoIP, their level of competition, the existence or absence of SMP and, in such case, the imposition of corresponding obligations and conditions".

covered by this notification. CMT has assigned numbers for the provision of VoIP services to only two companies, one of which is TESAU, and there is a risk that the latter may foreclose the VoIP market in the future.

CMT should closely monitor the development of IP-telephony services, to gather the relevant data which will allow CMT to carry out an accurate substitution analysis, and to re-evaluate its impact on the relevant markets within one year at the latest. Should such analysis affect its conclusion, CMT has to intervene accordingly by reviewing its market analysis⁹.

Pursuant to Article 7(5) of the Framework Directive, CMT must take the utmost account of comments of other NRAs and the Commission and may adopt the resulting draft measure and, where it does so, shall communicate it to the Commission.

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

Pursuant to Point 12 of Recommendation 2003/561/EC¹⁰ the Commission will publish this document on its website. The Commission does not consider the information contained herein to be confidential. You are invited to inform the Commission¹¹ within three working days following receipt whether you consider, in accordance with Community and national rules on business confidentiality, that this document contains confidential information which you wish to have deleted prior to such publication. You should give reasons for any such request.

Yours faithfully,
For the Commission,
Viviane Reding
Member of the Commission

⁹ To be notified in accordance with Article 7(3) of the Framework Directive.

¹⁰ Commission Recommendation 2003/561/EC of 23 July 2003 on notifications, time limits and consultations provided for in Article 7 of Directive 2002/21/EC, OJ L 190, 30.7.2003, p. 13.

¹¹ Your request should be sent either by email: INFSO-COMP-ARTICLE7@cec.eu.int or by fax: +32.2.298.87.82.