Wholesale call origination services provided over fixed networks

Identification and Analysis of Markets, Determination of Market Power and Setting of Remedies

Response to Consultation and Final Decision

18th January 2010

Contents

Executive Summary

The MCA is hereby presenting a decision following the market review on the market for wholesale call origination services provided over fixed networks. The national consultation period was held from the 27th May till the 31st July 2009, to which the MCA received one response from Vodafone Malta Ltd.. The respondent stated that it agreed with the findings of this market review in its entirety.

The draft decision was notified to the EU Commission on 23rd September 2009. On the 22nd October 2009 the EU Commission approved the draft decision. The EU Commission highlighted the importance of keeping the effectiveness of the remedies under constant monitoring to enable retail undertakings to compete in the market.

Background to previous analysis

The EU Commission refers to wholesale call origination on fixed networks as a candidate market susceptible for ex ante regulation. Wholesale call origination is a necessary input for alternative operators wanting to start offering retail call services without deploying their own network.

In 2006, during the first round market review for wholesale call origination services the MCA concluded that all networks capable of providing wholesale call origination where included in the market. The market included self-supplied wholesale call origination and services provided to third parties.

In its market analysis the MCA designated GO as having SMP in the provision of wholesale call origination services.

Given the position held by GO, the MCA identified a number of competition problems that could potentially arise. In this regard the MCA imposed on GO a number of regulatory obligations including access, non-discrimination, transparency, price control and cost accounting, and accounting separation.

Conclusions of this review

Identification of Markets

The MCA is defining call origination services as services on the public telephone network provided at a fixed location including call set-up, switching and connection for the initial stage of the call. It incorporates conveyance from an end-user to the next stage in the call routing (either call termination or to the point of interconnection).

Following a demand and supply side substitution analysis the MCA established that the market for wholesale call origination market includes:

- wholesale call origination services provided to third parties; and
- self-supplied wholesale call origination services.

The relevant market includes wholesale call origination services provided over public fixed electronic communications networks including the copper, cable and BWA networks.

The relevant geographic markets for the provision of wholesale call origination services is national in scope.

Further details on the MCA's market definition exercise can be found in **Chapter 2** to this document.

Assessment of Significant Market Power (SMP)

Following the identification of the market, the MCA carried out an analysis to determine whether any operator present in the said market enjoys SMP. The analysis indicates that GO enjoys significant market power in the wholesale call origination market. This position is likely to persist during the timeframe of this review.

The conclusion of dominance is supported by a number of factors including:

- high market share in terms of fixed lines and volumes of minutes;
- vertically integrated provider;
- overall size;
- economies of scale and scope; and
- no countervailing buyer power.

Full details of the MCA's assessment of SMP can be found in **Chapter 3** of this document.

Regulatory Obligations

Given the finding of SMP, the MCA is obliged to impose remedies on the identified SMP operator. The MCA is therefore imposing the following obligations on GO:

a. Access to wholesale call origination and associated services;

b. Non-discrimination;

c. Transparency;

d. Accounting separation; and

e. Price control and cost accounting.

The MCA believes that the above regulatory obligations are based on the nature of the competition problems it has identified in the relevant market, and that each obligation is proportionate and justified.

Full details of the MCA's regulatory measures, are contained in **Chapter 4** to this document.

Chapter 1 Introduction

The EU regulatory framework for electronic communications networks and services entered into force in Malta on the 14th September 2004. The framework is designed to create harmonised regulation across Europe and is aimed at reducing entry barriers and fostering prospects for effective competition to the benefit of consumers. The basis for the regulatory framework are five EU Communications Directives:

- Directive 2002/21/EC on a common regulatory framework for electronic communications networks and services (“the Framework Directive”);
- Directive 2002/19/EC on access to, and interconnection of, electronic communications networks and associated facilities (“the Access Directive”);
- Directive 2002/20/EC on the authorisation of electronic communications networks and services (“the Authorisation Directive”);
- Directive 2002/22/EC on universal service and users' rights relating to electronic communications networks and services (“the Universal Service Directive”); and
- Directive 2002/58/EC concerning the processing of personal data and the protection of privacy in the electronic communications sector (“the Privacy Directive”).

The Framework Directive provides the overall structure for the regulatory regime and sets out fundamental rules and objectives, which read across all the directives. Article 8 of the Framework Directive sets out three key policy objectives, which have been taken into account in the preparation of this consultation document, namely promotion of competition, development of the internal market and the promotion of the interests of citizens of the European Union.

The Maltese legislation transposing these Directives came into effect on the 14th September 2004. The relevant pieces of legislation are the Electronic Communications (Regulation) Act, 2004 (hereinafter referred to as ECRA) and the Electronic Communications Networks and Services (General) Regulations, 2004 (hereinafter referred to ‘ECNSR’).

The Directives require National Regulatory Authorities (NRAs) such as the MCA to carry out reviews of competition in communications markets to ensure that regulation remains appropriate in the light of changing market conditions.

Each market review is divided into three main parts:

- definition of the relevant market or markets;
- assessment of competition in each market, in particular whether any companies have Significant Market Power (SMP) in a given market; and
- assessment of the appropriate regulatory obligations which should be imposed, given the findings on SMP (NRAs are obliged to impose some form of regulation where there is SMP).

More detailed requirements and guidance concerning the conduct of market reviews are provided in the Directives, the ECRA, the ECNSR and in additional documents issued by the European Commission and the MCA. As required by the new regime, in conducting this review, the MCA has taken the utmost account of the two European Commission documents discussed below.

1.1 Market review methodology

In 2003 the EU Commission published its first Recommendation on relevant markets, which identifies a set of eighteen markets in which ex ante regulation may be warranted. The Recommendation seeks to promote harmonisation across the European Community by ensuring that the same product and service markets are subject to a market analysis in all Member States. However, NRAs are able to regulate markets that differ from those identified in the Recommendation where this is justified by national circumstances. Accordingly, NRAs are to define relevant markets appropriate to national circumstances, provided that the utmost account is taken of the product markets listed in the Recommendation (Regulation 6 of the ECNSR).

In December 2007 the EU Commission adopted its revised Recommendation on relevant markets. The revised Recommendation presents a much short list of markets which NRAs are required to analyse for the purpose of ex ante regulation.

The European Commission has also issued guidelines on market analysis and the assessment of SMP ("SMP Guidelines"). The MCA has also published a document outlining the guidelines on the methodology to be used for assessing effective competition in the Maltese electronic communications sector[1]. The MCA is required to take these guidelines into utmost account when analysing a product or service market in order to assess whether the market under investigation is effectively competitive or otherwise (refer to Regulation 8 of the ECNSR).

As required by Regulation 6 of the ECNSR, the results of these market reviews and the proposed draft measures need to be notified to the European Commission and to other NRAs. The Commission and other NRAs may make comments within the one month consultation period. If the Commission is of the opinion that the market definition, or proposals to designate an operator with SMP, or proposals to designate no operator with SMP, would create a barrier to the single market, or if the Commission has serious doubts as to its compatibility with Community law and issues a notice under Article 7(4) of the Framework Directive, the MCA is required by Regulation 6 of the ECNSR to delay adoption of these draft measures for a further period of 2 months while the Commission considers its position.

The MCA has collected market data from a variety of internal and external sources, including providers of electronic communications networks and services, in order to carry out thoroughly its respective market definition and market analysis procedures based on established economic and legal principles. The MCA is also taking the utmost account of the Recommendation on relevant markets and the SMP Guidelines.

1.2 Liaison with Competition Authority

Under Regulation 10 of the ECNSR, there is a requirement on the MCA to carry out an analysis of a relevant market within the electronic communications sector. This analysis must be carried out in accordance, where appropriate, with an agreement with the National Competition Authorities (NCA) under Regulation 10 of the ECRA.

[1] Link to market review methodology: http://www.mca.org.mt/infocentre/openarticle.asp?id=513&pref=1

In line with the cooperation agreement signed on the 20th May 2005 between the MCA and the Office of Fair Competition (OFC)[2], the MCA has initiated a two-week consultation process with the OFC. The MCA has forwarded and presented the results of this review to the OFC. The OFC agrees with the conclusions of this review and its official position is available in Appendix 1 to this document.

1.3 Structure of the document

The rest of the document is structured as follows:

Chapter 2 presents the MCA's conclusions on the definition of the market for the wholesale call origination on fixed networks in Malta;

Chapter 3 presents the MCA's market analysis for the market identified and outlines whether this market is effectively competitive or not; and

Chapter 4 provides a discussion of the general principles associated with the imposition of remedies.

1.4 Scope of this review

This review considers the market for wholesale call origination services provided over fixed networks in Malta.

[2] http://www.mca.org.mt/infocentre/openarticle.asp?id=656&pref=9

Chapter 2 Market Definition

2.1 Introduction

Regulation 10 of the ECNSR provides that before an SMP determination may be considered, the MCA must identify the markets in relation to which it is appropriate to consider such a determination and to analyse those markets. In identifying the relevant markets, the MCA is required to take utmost account of all applicable guidelines and recommendations issued by the European Commission.

There are various dimensions related to the market definition procedure. Paragraph 2.1 of the Commission's Recommendation on relevant markets (Explanatory Note) states that *'As the market analysis carried out by the NRAs have to be forward-looking, markets are defined prospectively. Their definitions take account of expected or foreseeable technological or economic developments over a reasonable horizon linked to the timing of the next market review'*. In this regard, the MCA carries out its market analysis on a forward looking basis, and where it is thought possible that market conditions may change significantly during the timeframe of this review, these changes are identified and discussed.

The Commission identified the wholesale call origination market as a relevant market for assessment by the NRAs. It includes the originating access that enables providers to supply retail calls on the public fixed telephone network.

The MCA has conducted an assessment of the market for wholesale call origination on fixed networks in order to validate its appropriateness in the Maltese context, and as preparatory work for the assessment of SMP in this market.

Where the market definition differs from the Commission's Recommendation the differences are identified and justification given in the light of the national circumstances which justify this departure, in the manner prescribed by the Commission's Recommendation.

2.2 Background on fixed telephony networks

In Malta, there are three ubiquitous networks currently providing fixed telephony services at retail level. The incumbent fixed operator GO plc. operates an IP fixed telephony network based on an NGN setup. Melita plc. operates a hybrid fibre coaxial (HFC) cable network over which it provides IP telephony services. In 2008 Vodafone Malta Ltd. started offering a fixed telephony service, in conjunction with broadband services, over its WiMax network using the fixed broadband standard (D-standard). Apart from these network operators there is also Sky Ltd. which is offering fixed telephony services as a Carrier Select and Pre-select (CS and CPS) operator hosted on GO's network.

As from 2006 the incumbent operator GO upgraded its fixed PSTN network to an NGN network. Since NGNs rely on packet-based rather than circuit-switched solutions, NGNs are more streamlined in the way they convey calls. GO is able to cover the national territory with four fully-meshed media gateways as opposed to the fifteen PSTN switches previously in operation.

The cable infrastructure is also deployed in an NGN setup. Melita's cable network has ubiquitous coverage of Malta. Its network is a typical bi-directional hybrid fibre coaxial (HFC) cable network. In 2000, Melita started offering high speed Internet access across its HFC network via cable modem and as from July 2005 it also introduced a packet-based voice service. Melita has concluded interconnection agreements with all other local fixed and mobile operators

Vodafone Malta Ltd deployed the first BWA network in Malta using the WiMax D-standard and started offering retail broadband and fixed telephony services in June 2008. Its network setup is also based on an NGN setup and has a national coverage. Another nationwide BWA network has been deployed by Go Mobile (the mobile arm of GO plc), however up to day remains unutilised.

Siscom Ltd. operates a fixed network in the private area of Tigne Point Development. This operator provides self-supplied wholesale call origination for the purpose of providing retail call services to its clients within the private area. This operator has an interconnection agreement with GO only, and uses transit services from GO to terminate calls on other fixed and mobile operators. The MCA considers that given the small geographic footprint and the very small number of end-users serviced by Siscom, there is no scope for further detailed consideration of this operator in the analysis. Given the particular nature of this operator there is no scope for any alternative operator to seek wholesale access and call origination services from Siscom. In any event the inclusion of this operator in the analysis would not have changed the findings of this review in any way.

2.3 Wholesale Markets Boundaries

Since all public fixed networks in Malta are packet-based, the concept of tandem switching does not apply to NGNs.

Based on this, the MCA is defining the boundaries of the relevant markets for call origination, call termination and transit services as follows:

Call origination services on the public telephone network provided at fixed locations include call set-up, switching and connection for the initial stage of the call. They incorporate conveyance from an end-user to the next stage in the call routing (either call termination or to the point of interconnection).

Call termination provides call completion and switching functionality at the terminating end of a call. It involves the conveyance of calls from the end of the previous stage (either call origination or to the point of interconnection), to the called end-user via the local loop.

Transit services comprise the pure conveyance of calls between two operators across a third transit operator. This incorporates both national and international calls.

These market boundaries are depicted in the diagram below.

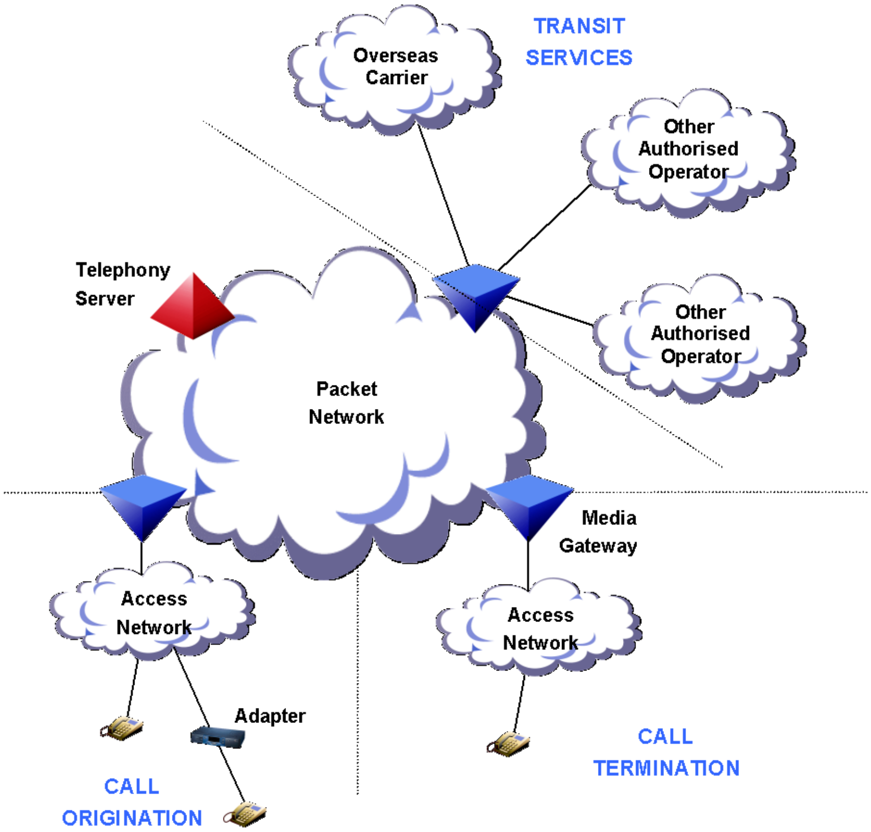

Figure 1 - NGN Market Boundaries

2.4 Market Definition Process

The purpose of the market definition process is to identify the competitive constraints that electronic communications service providers face. There are two dimensions to the definition of a relevant market: the relevant products to be included in the same market and the geographic extent of the market. The MCA's approach to the market definition is in line with that identified in the MCA's market review methodology.

Recital (4) of the Recommendation clearly states that the starting point for market definition is a characterisation of the retail market over a given time horizon, taking into account the possibilities for demand and supply-side substitution. The wholesale market is then identified subsequently to this exercise being carried out in relation to the retail market.

This review will only focus on the aspects of wholesale call origination services. For the purpose of this document call origination services on the public telephone network provided at fixed locations include call setup, switching and connection for the initial stage of the call. They incorporate conveyance from an end-user to the next stage in the call routing (either call termination or to the point of interconnection).

2.5 Retail Market

The Explanatory Memorandum to the Commission's Recommendation on relevant markets states that *'the relevant market is considered to comprise call origination for* *telephone calls and for the purpose of accessing dial-up internet service provision'.* Since the demand for wholesale call origination services is derived from the demand for retail services, the MCA takes the view that the scope of the wholesale market definition is conditioned by the extent to which operators require call origination services to be able to provide the relevant range of retail services. The MCA has first considered the relevant retail markets and then analysed those at the wholesale level.

The demand for call origination stems from:

- carrier selection (CS), carrier pre-selection (CPS) and other directly related services such as the wholesale line rental (WLR); and
- the demand for call services by subscribers of the access network operators.

The analysis of the retail markets in the document on *'National Telephone Services Provided At Fixed Location'*[3], led to the view that service providers offering telephone services tend to offer end-users an entire range of call types. These would generally include calls to geographic numbers, calls to non-geographic numbers, international calls, dial-up Internet calls and calls to mobile. The call origination services in this analysis are therefore being defined by reference to such retail telephone call services.

To offer retail call services, service providers require the ability to offer access services to fixed networks. An important facility that CS and CPS operators require to be able to match the full retail offering of the network provider is wholesale line rental. Through WLR a service provider can offer both access and calls to the end-user, which facilitates the way the end-user acquires and pays for the fixed call services.

In the market analysis of the retail calls and access markets the MCA concluded that the distinction between residential and non-residential customers is fading quickly and there is no evidence that such a distinction is required anymore. At wholesale level this distinction is also not applicable. Wholesale call origination services provided to competing undertakings are the same regardless of whether they are being provided in relation to residential or business subscriber lines. This suggests that wholesale call origination for residential and business subscribers falls within the same market.

2.6 Wholesale Market

2.6.1 Wholesale Demand Side Substitutability

Wholesale call origination can either be self-supplied by a network operator to its own retail arm or provided to third parties. These third parties can be CS/CPS operators, terminating providers of non-geographic services (for example freephone services provided by alternative operators), and Internet Service Providers.

Only the operator with control over the end-user connection can provide call origination services. An alternative operator wanting to provide CS/CPS services to the customers currently subscribed to operator X cannot resort to call origination services from operator Y as a feasible substitute to call origination services of operator X. Nevertheless, the CS/CPS may decide to switch to an alterative network for the provision of call origination services and target the subscribers of that network, following a price increase in wholesale call origination by operator X. The feasibility of such a switch would depend on a number of factors mainly the extent of network coverage, the number of retail connections of the network operator (therefore the potential retail market for the CS/CPS

[3] Link to document: http://www.mca.org.mt/newsroom/openarticle.asp?id=713

operator), reliability of the network, and the willingness of the network operator to provide wholesale services to the CS/CPS operator.

An increase in the price of wholesale call origination would be passed on to the retail level. Such an increase would be passed on to both the retail arm of the network operator and third parties acquiring wholesale call origination. Nevertheless, the network operator offering wholesale call origination would face reduced revenues at retail level but higher revenues at wholesale level, thus simply shifting the revenues from the downstream to the upstream level. For the third party retail service provider an increase in the charges of wholesale call origination would either mean lower retail revenues if it absorbs the price increase, or end up charging higher retail prices to the end-user if it decides to pass on the price increase. This puts the wholesale provider in a better situation to compete than the third party service provider.

The end-user has the ability to choose its originating operator[4] predominantly based on the level of pricing at the retail level. If the increase in retail costs is significant, the end-user will most likely switch retail service provider. The ability on the part of the end-user, to switch to another network operator or CS/CPS operator imposes a pricing constraint on the wholesale call origination price offered by an access network operator. This suggests that different network operators offering retail call services fall within the same market for the purposes of wholesale call origination.

One direct alternative to the purchase of wholesale call origination is to establish network access to end-user locations by building a new network. Whilst building a new network may be an option to consider, a new entrant is likely to find it very difficult to deploy such a network due to the high investment costs involved. A small new entrant would see these start-up costs as too high compared to the relatively cheaper option of acquiring wholesale call origination services from an existing operator. It would be more practical for the new entrant to first start with acquiring a customer base using such a wholesale solution and then decide to move up the ladder of investment.

A new entrant may also decide to purchase or lease an established network connection to the end-user locations. This may be done by, for example, by renting local loops or acquiring leased lines. The MCA believes that neither of these alternatives is a suitable substitute for call origination. Such services are not functionally equivalent to wholesale call origination in that they provide dedicated access to the end-user. This is also reflected in their higher cost compared to wholesale call origination. Whilst in the case of wholesale call origination the service provider pays only for the switched capacity, the acquisition of leased lines and unbundled local loops requires a substantial financial commitment. The MCA therefore considers it unlikely that service providers would promptly switch between wholesale call origination services and leased lines or unbundled local loops, in response to a 5 to 10% increase in price.

The MCA therefore considers that there is enough level of substitution at wholesale and retail level to consider all networks providing wholesale fixed call origination services to fall within the same wholesale market, independently of the underlying technology being used.

2.6.2 Wholesale Supply Side Substitutability

In considering supply-side substitution, the key question to ask is whether a prospective supplier would enter the market in response to a small but significant increase in the price of wholesale call origination by a hypothetical monopolist.

[4] The calling party can choose either the retail arm of the network operator, a CPS operator, or another network operator offering access and call services

As explained earlier, a ubiquitous bi-directional cable infrastructure, which currently covers more than 95 per cent of all households, has been operating since 1991. Together with the provision of television and broadband data services the cable operator offers IP telephony services. The cable operator has concluded interconnection agreements with all other network operators. Since the cable operator has already started offering wholesale call services as a self-supply service there is limited scope to observe supply side substitution.

Another alternative type of access network is broadband wireless access (BWA) network. In October 2005, the MCA allocated frequency spectrum to three undertakings for the deployment of national BWA networks. One of these operators, Vodafone have deployed the WiMax network and have started offering broadband and IP telephony services since June 2008. As with the case of the cable network, supply side substitution for BWA is not possible to observe since it is already providing wholesale call origination.

Based on these facts it is therefore appropriate to consider wholesale call origination over the cable and BWA networks to be in the same relevant market as that of the traditional copper based network.

2.7 Relevant Geographic Market

A relevant geographical market comprises the area in which the undertakings concerned are involved in the supply and demand of products and/or services, in relation to which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different to those areas.

According to the EU Guidelines, in the electronic communications sector, the definition of the geographical scope of the relevant market is generally determined with reference to the area covered by a network, and to the existence of legal and other regulatory instruments.

Based on these definitions and the market conditions described earlier on the MCA takes the view that the relevant geographic market for the provision of wholesale call origination services is national in scope. This view is supported by the fact that all fixed networks operate at a national level and do not differentiate their services in terms of pricing and availability between different geographic regions.

2.8 Identified Markets

The MCA defines call origination services as services on the public telephone network provided at a fixed location including call set-up, switching and connection for the initial stage of the call. It incorporates conveyance from an end-user to the next stage in the call routing (either call termination or to the point of interconnection).

Based on the analysis presented above, the MCA is hereby identifying the relevant market for wholesale call origination to include:

- wholesale call origination services provided to third parties; and
- self-supplied wholesale call origination services.

The relevant market includes wholesale call origination services provided over public fixed electronic communications networks including the copper, cable and BWA networks.

Chapter 3 Market Analysis

After having identified the relevant market, the MCA is required to analyse the market in order to assess whether any service provider/s hold significant market power as defined in Regulation 8 of the ECNSR (Article 14 of the Framework Directive).

3.1 Method to Assess Significant Market Power

Under the EU Communications Directives and Article 8(2) of the ECNSR, SMP has been defined so that it is equivalent to the competition law concept of dominance. The ECNSR defines states that:

"An undertaking shall be deemed to have significant market power either individually or jointly with others if it enjoys a position equivalent to dominance, that is to say a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers."

Article 8(4) of the ECNSR introduces the concept of leveraging of market power and states that:

"*Where an undertaking has significant market power on a specific market, it may also be deemed to have significant market power on a closely related market, where the links between the two markets are such as to allow the market power held in one market to be leveraged into the other market, thereby strengthening the market power of the undertaking*".

Therefore, in the relevant market, one or more undertakings may be designated as having SMP where that undertaking, or undertakings, enjoys a position of dominance. Also, an undertaking may be designated as having SMP where it could lever its market power from a closely related market into the relevant market, thereby strengthening its market power in the relevant market.

In assessing whether an undertaking has SMP, this review takes the utmost account of the Commission's SMP Guidelines as well as the MCA's equivalent guidelines

3.2 Assessment of SMP against Relevant Criteria

This section considers whether single dominance is likely to exist in the identified relevant market. In the MCA's view the assessment is fully compliant with the Commission's Guidelines. The SMP assessment is based on the evidence available to the MCA.

Single dominance can be assessed using a large number of criteria as described in the Commission's and the MCA's guidelines on SMP assessment. This analysis in the first instance considers the following key criteria:

- Market share analysis;
- Size of the undertaking;
- Barriers to entry;

- Countervailing buyer power;
- Vertical Integration.

3.2.1 Analysis of Market Shares

Although high market shares are not in themselves decisive as to whether an undertaking enjoys SMP in a market, the MCA is of the opinion that market shares higher than 50 per cent would necessitate the designation of SMP. Paragraph 75 of the Commission Guidelines states that, *"according to established case-law, very large market shares – in excess of 50% - are in themselves, save in exceptional circumstances, evidence of the existence of dominant position."*

Until June 2005, GO (Maltacom at that time) was the only provider of fixed access and calls in Malta and was therefore the only provider that was present at both retail and wholesale level. Following this date new operators entered the market and started providing fixed telephony services as depicted below.

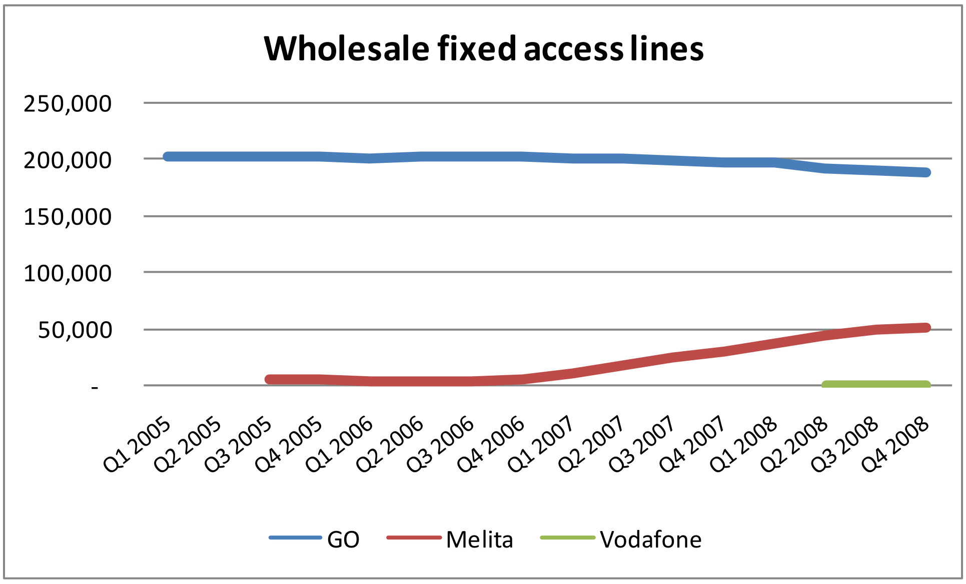

Figure 2

In June 2005 Melita started offering fixed telephony service but this service was only provided as an add-on to broadband or television packages. Furthermore, this telephony service was only available for the purposes of on-net calls, given that at the time Melita did not have interconnection agreements in place. Due to these two main limitations the number of subscribers to this telephony service were minimal. By the end of 2006 Melita concluded interconnection agreements with other operators and started offering its telephony service as a stand-alone service. Since then, the number of customers subscribing to the Melita fixed telephony service increased over time and now stand at around 50,000.

Following the deployment of a WiMax network Vodafone started offering fixed telephony service only as an add-on to its broadband packages. To date the take up of this service is negligible, mainly due to the fact that customers wanting to acquire fixed telephony service from Vodafone need to purchase a broadband service. The additional cost of getting a broadband connection makes the telephony service comparatively more expensive to Melita's or GO's service.

In terms of market share of access lines GO maintains the highest market share with more than 78% of fixed access lines. Melita has 21% and Vodafone has just 0.2% of access lines as at December 2008. Table 1 below illustrates the evolution of market share in terms of wholesale fixed lines.

	Q4 2005	Q4 2006	Q4 2007	Q4 2008
GO	97.3%	97.1%	86.9%	78.6%
Melita	2.7%	2.9%	13.1%	21.2%
Vodafone	0.0%	0.0%	0.0%	0.2%

Table 1

One interesting factor to note is that whilst the market share of GO has declined by 20% over a three year period, its fixed line connections in absolute terms have not declined much. In fact as depicted in the Figure 2 above the reduction in GO's fixed lines is not significant. When comparing GO's number of connections in Q1 2005 (when it was a monopolist), to the number of connections today, GO has only lost 8.5% of its connections.

Figure 3 below shows the evolution of originating minutes over fixed networks over time. During 2006 and 2007 the total minutes have decreased considerably mainly due to declines in Internet dial-up minutes, the high use of SMS and also because of people making less fixed calls in general. During 2008 this trend has reversed and fixed originating minutes have experienced an increase. The reason for this increase cannot be attributed to any particular reason, except perhaps that during 2008 packages included 'free' minutes gained more visibility with end-users.

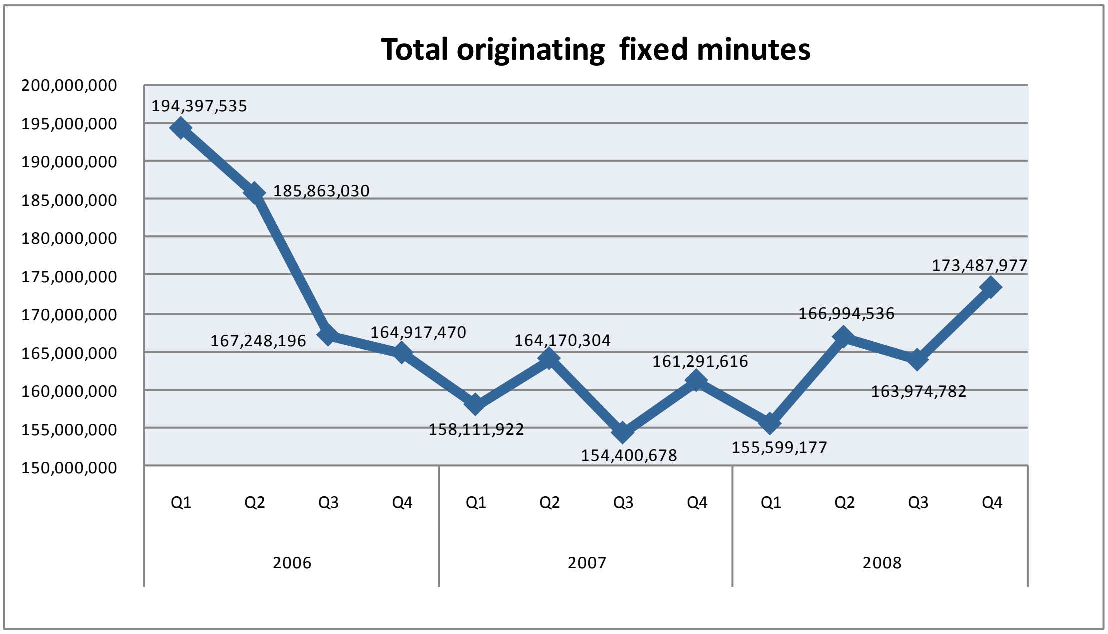

Figure 3

In terms of market share by volumes, as depicted in the table below, GO maintained a high market share of 75% of wholesale originated minutes.

	Q4 2005	Q4 2006	Q4 2007	Q4 2008
GO	99%	99%	83%	75.3%
Melita	1%	1%	17%	24.6%
Vodafone	0%	0%	0%	0.1%

Table 2

Table 2 shows that GO has a presumption of SMP in the provision of wholesale call origination services at a fixed location. The finding of dominance is further supported by the fact that GO has an enduring high market share in this market. Despite the entry of new operators providing call origination GO still maintains a very strong presence in the market. The MCA expects that this situation is likely to persist during the timeframe of this review.

3.2.2 Size of the undertaking

Undertakings having a large size relative to their competitors in a particular market may enjoy potential advantages, and sustain those advantages in a number of operational areas. Such advantages may also accrue in part due to other activities of the under-taking outside the market under consideration.

As shown in the market share analysis GO maintains nearly 80% of all retail fixed access lines and around 75% of all fixed line minutes originated on fixed networks. The second largest competitor is Melita with around 20% of the market share in lines and minutes. Besides its negligible market share Vodafone has the added disadvantage that it is not offering retail telephony services as a stand alone service. This further limits the scope for a CS/CPS operator to seek access from Vodafone.

For a CS/CPS operator seeking wholesale call origination services the size of the host network operator is probably the most important factor to consider. The larger the market presence of the host operator, the greater is the potential market for the CS/CPS operator. Therefore a CS/CPS operator would opt to seek wholesale access from the largest operator in the market.

An additional advantage for the CS/CPS operator in seeking the largest operator is that it can benefit from the economies of scale of the host network operator. If the network operator passes on its economies of scale to the service provider, than the CS/CPS operator would be in a better position to compete at retail level. Additionally, if the CS/CPS takes a WLR product such that it can provide an end-to-end retail product, it can also start competing with alternative network operators.

The MCA believes that in the absence of regulatory intervention, GO would be in a position to discriminate against smaller operators seeking wholesale call origination.

3.2.3 Barriers to entry

Barriers to entry can take many forms such as significant sunk costs or economies of scale and scope resulting from the presence of a large undertaking in the market. The presence of entry barriers are conducive for an operator to exercise market power.

Economies of scale

For a significant number of years, GO has been the only operator providing fixed access and telephone services in Malta. Given the ubiquity and the high density of its network, GO enjoys economies of scale in providing fixed access and call services. The per unit cost incurred by this undertaking for providing these services are therefore likely to be much lower than those of a new entrant which would need to obtain a large share of the market if it is to effectively compete with the incumbent. In order to gain a large market share the new entrant will have to price below the incumbent's prices, thereby making it very difficult for this operator to cover its costs.

The second largest operator in the market Melita also has a ubiquitous network and provides a full range of services. Melita's cable network is also a packet based network similar to GO and therefore it has the possibility to enjoy similar economies of scale in the provision of call origination services. Although Melita subscriber base has increased considerably over the past years, it is however still far from the number of subscribers and minutes registered by GO. This implies that GO is still better positioned to enjoy economies of scale.

Vodafone's WiMax network is a relatively new network and the ability of Vodafone to exploit economies of scale so far is limited by the few number of subscribers and volume of minutes generated on its network. Nevertheless, given that the WiMax network is also packet based there is the possibility that in the future Vodafone will also start exploiting such economies of scale.

Given the present market maturity any new entrant bound to enter the market at this point will find it difficult to gain sufficient market share to enjoy significant economies of scale such as GO. The deployment of a new fixed network, whilst possible, still poses significant sunk cost and long timeframes, such that it will make it difficult for new market entrants to compete with GO.

Economies of scope

Economies of scope exist where average costs for one product are lower as a result of it being produced jointly with another product by the same firm. Cost savings may be made where common processes are used in the provision of a group of services. When an operator is present in a large number of markets it can share common costs over a greater range of services.

GO is present in a large number of electronic communications markets providing a full range of services over its ubiquitous network, such as leased lines, international connectivity, fixed calls and other services. Melita is also a horizontally integrated operator offering different services to its customers. With respect to economies of scope Melita is in the same position as GO, in that for its fixed customers it can gain advantage from the fact that it also offers other services such as broadband and television. Vodafone limited footprint in the fixed market makes it very unlikely that it is at present enjoying any benefits from economies of scope.

The ability to benefit from economies of scope may act as a barrier to entry for new competitors. For a new entrant to enjoy such economies of scope it would need to enter a large number of markets simultaneously, which would firstly increase the entry costs and secondly would make it more difficult to recoup such costs on exit. The MCA believes that given the presence of high economies of scale and scope acts as a barrier to entry.

The MCA believes that considering the size of GO relative to the other operators and any potential new entrant, the market present barriers to entry. GO large market share enables it to benefit from significant economies of scale and scope.

3.2.4 Vertical Integration

Vertical integration involves an undertaking operating in a given market, while also being present in a market that is at a higher or lower level in the chain of provision. Since vertically integrated operators are able to influence both upstream and downstream markets it would be more difficult for a new provider entering in one of these markets to compete effectively with the integrated operator.

All operators present in this market are vertically integrated operators and operate at a wholesale and retail level. Melita and Vodafone provide self-supply wholesale call origination services to provide retail call services, whilst GO provides self-supply wholesale call origination services internally and to an independent CS/CPS operator Sky Telecom.

The ability to leverage market power from upstream to downstream markets may deter potential entry in these markets. An integrated provider can make it difficult for new entrants at a retail level to obtain the necessary inputs at a competitive price (i.e. cost based) and therefore create an entry barrier at retail level.

In the absence of wholesale regulation, GO would have the ability to raise wholesale call origination charges whilst keeping its retail charges the same. This would allow GO to remain competitive at retail level and maintain the same level of revenue overall, whilst the CS/CPS operator would have to either absorb the increase in costs or pass it on to the end-user. In both cases the CS/CPS operator is worse off due to the price increase.

In case of the price increase the CS/CPS operator can also decide to switch to another operator to get wholesale call origination at a cheaper price. However since GO has the largest retail market share the CS/CPS operator might not find it feasible to switch to an operator with a much smaller market share. The CS/CPS operator's customer base is the same as that of the wholesale operator hosting it, and therefore the large the retail market share of the wholesale operator the bigger are the possibilities for the CS/CPS operator to gain a higher retail market share. This factor limits the incentive for the CS/CPS operator to switch to other networks following a price increase in wholesale call origination.

The MCA believes that this situation at a wholesale level will persist during the timeframe of this review and in the absence of appropriate regulation.

3.2.5 Countervailing Buyer Power

The existence of customers with a strong negotiating position, which could be exercised to produce a significant impact on competition, will tend to restrict the ability of providers to act independently of their customers. The extent of countervailing buyer power depends on the ability of large customers to switch to alternative providers or not to purchase the service or product from that particular provider within a short period of time.

As stated before, although in Malta there are three networks capable of providing wholesale call origination, GO remains by far the largest operator providing wholesale call origination services. At present Sky Telecom is the only alternative operator currently purchasing wholesale call origination services from GO.

Given that GO has the largest number of retail subscribers it is reasonable to believe that Sky has an incentive to stay on GO's network since moving to another wholesale call origination provider would result in a small potential retail customer base. Consequently, given the size of GO, Sky is not in a position to exert countervailing buyer power on GO. Sky requires call origination services from GO and is therefore a price taker.

Within the current market structure the MCA believes that CS/CPS operators lack the ability to exercise countervailing buyer power on GO in setting wholesale call origination charges.

3.3 Conclusion and SMP designation

Based on the analysis presented above the MCA believes that GO enjoys significant market power in the wholesale call origination market. This position is likely to persist during the timeframe of this review.

The conclusion of dominance is supported by a number of factors including:

- high market share in terms of fixed lines and volumes of minutes;
- vertically integrated provider;
- overall size;
- economies of scale and scope; and
- no countervailing buyer power.

Chapter 4 Regulatory Measures

Regulation 10(4) of the ECNSR states that, where an operator is designated as having significant market power in a relevant market in accordance with Regulation 8 of the same ECNSR, the MCA shall impose, or amend if already imposed, the most appropriate of the following obligations:

- Transparency (Regulation 18)
- Non-discrimination (Regulation 19)
- Accounting Separation (Regulation 20)
- Access to, and use of, specific network facilities (Regulation 21)
- Price control and Cost Accounting (Regulation 22)

In addition to the above, Regulation 17(3) of the ECNSR empowers the MCA, in exceptional circumstances, to propose the imposition of additional access or interconnection obligations on an operator with SMP. In doing so, the MCA is required to obtain authorisation from the European Commission prior to imposing said obligations.

Any obligations imposed by the MCA upon an operator with SMP in accordance with the above must:

- be based on the nature of the problem identified;
- be proportionate and justified in the light of the objectives laid down in article 4 of the ECRA; and
- only be imposed following consultation in accordance with article 10 of the ECRA and regulation 6 of the ECNSR.

This section aims at discussing the potential competition problems that can exist in the wholesale call origination market, and impose adequate remedies to address these problems.

4.1 Current Remedies

In the first round market review of the wholesale call origination market the MCA had determined GO (at the time Maltacom) as having SMP. Consequently the MCA had imposed on GO the following remedies:

- To provide third parties with access to the required network access and facilities for the acquiring of wholesale call origination services – in particular CS/CPS and WLR services;
- Ensure that the access or service provided are provided on a transparent and non discriminate basis;
- Apply a cost oriented price system for the charging of wholesale call origination; and
- Maintain an accounting separation system which enables the MCA to monitor cost and revenue allocations between different services offered by GO.

4.2 Potential Competition Problems

The MCA has identified a number of potential SMP-related competition problems in the wholesale fixed call origination market under review. These are leveraging (vertical and horizontal), barriers to entry and price-related problems.

4.2.1 Leveraging

Vertical leveraging is the practice of a dominant firm that denies proper access to an essential input that it provides with the intent of extending its power from one segment of the market (the bottleneck segment) to the other (the potentially competitive segment). Such practice may be both price-related and/or otherwise.

GO, as a vertically integrated operator which is dominant in an upstream market may, unless prohibited by effective regulatory intervention, engage in pricing that gives rise to a margin squeeze. Furthermore, since it is able to access economies of scale and scope that are not so readily available to potential undertakings competing at the downstream level, the said undertaking may bring extra pressure to bear on the margins available for competing downstream operators. GO may also resort to other price leveraging strategies such as price discrimination and cross-subsidisation.

Over and above such price leveraging strategies, unless prohibited by effective regulation, GO may engage into other forms of non-price leveraging such as, discriminatory use or withholding of information, delaying tactics, quality discrimination and the imposition of undue requirements on, and with respect to, alternative service providers.

Currently, the wholesale rates which GO applies are regulated and this has mitigated the aforementioned competition problems to a certain extent. The MCA considers that further regulation at wholesale level is essential in order to mitigate price-related problems at both wholesale and retail level.

Horizontal leveraging involves the dominant undertaking using its position in one market to exert undue influence on other markets at the same level in the value chain. This form of leveraging can be exercised by GO as it operates in a number of horizontal wholesale markets and can potentially leverage its power from one market to another.

4.2.2 Barriers to entry

Besides the leveraging issues discussed above, the MCA believes that the SMP position held by GO in the wholesale market under review may gives rise to problems related to entry deterrence.

As discussed in the market analysis, the MCA notes that currently GO enjoys a high market share in the wholesale call origination market. Furthermore, given its size GO enjoys economies of scale in the provision of wholesale and retail call services.

The MCA believes that given the position of GO in the market it can, in the absence of regulation, make it difficult for alternative operators to enter the market and acquire wholesale call origination. Furthermore, given that GO is also competing at retail level it has a further incentive to make it difficult for alternative operators to acquire wholesale services.

4.2.3 Price related problems

A major issue that may arise in the absence of regulation is price related problems in the provision of wholesale call origination services. Given that GO operates at wholesale and retail level in the provision of fixed calls, problems such as excessive wholesale prices and/or predatory pricing at retail level to foreclose competition at downstream markets may arise.

GO is in a position to engage in price squeeze and/or discrimination practices, as well as cross-subsidisation, in order to foreclose the retail market and gain advantage over smaller retail operators.

Since it is not envisaged that during the timeframe of this review, the market for wholesale call origination will become effectively competitive, in order to bring the benefits of competition to the end-user and to reduce market failures associated with the foreclosure of retail markets, it is essential that competing operators can gain access to GO's infrastructure. This implies that remedies should be imposed in order to provide alternative operators with essential wholesale inputs.

4.3 Principles Applied in Selecting Remedies

Given the identified potential competition problems arising from SMP in the market under review, the MCA is obliged to impose obligations on undertakings identified by it as having significant power on those markets. Accordingly, the MCA is imposing those appropriate obligations that it believes will encourage efficient entry in the market under review.

As discussed earlier, in selecting the remedies to impose on the designated SMP operator, the MCA considered the nature of the problem identified and, in accordance with the principle of proportionality, where necessary, is imposing those remedies which it considers to be the least burdensome, yet most effective. The MCA also took account of potential effects on any related markets especially downstream markets.

The MCA notes that it is unlikely that any single remedy can achieve the aim of ensuring that the competition problems identified above are effectively mitigated. Hence, the need for a suite of remedies that complement, support and reinforce each other.

4.4 Regulatory Obligations

The MCA has identified GO as having SMP in the wholesale call origination market and is therefore imposing appropriate remedies on the said undertaking.

The MCA is of the opinion that the remedies it is imposing are based on the nature of the competition problems it has identified in the relevant market and are proportionate and justified in light of the objectives set out in Article 4 of the Electronic Communications (Regulation) Act.

The MCA will however continue to monitor market developments and, where appropriate, may issue further directions refining these remedies.

4.4.1 Access

As described above, due to GO's SMP status in the wholesale call origination market, the placing of an effective access obligation on Maltacom is deemed necessary. Without the imposition of such an obligation, negative and anti-competitive effects can be experienced in the retail markets. The MCA considers that the denial of access to third parties by GO or the provision of access on unreasonable terms and conditions having a similar effect would hinder competition at the retail level and would not be in the end-user's interest.

In accordance with Regulation 21 of the ECNSR the MCA is therefore requiring GO to abide by the obligation to provide wholesale access for call origination and associated services.

When imposing such access obligations, the MCA may also attach to such obligations conditions of fairness, reasonableness and timeliness as required under Regulation 21(3) of the ECNSR.

Notwithstanding this, in accordance with the principles of proportionality, when considering which of the access obligations, if any, to impose, the MCA in accordance with Regulation 21(4) is required to take into account of the following:

(a) the technical and economic viability of using or installing competing facilities, in the light of the rate of market development, taking into account the nature and type of interconnection and access involved;

(b) the feasibility of providing the access proposed, in relation to the capacity available;

(c) the initial investment by the facility owner, bearing in mind the risks involved in making the investment;

(d) the need to safeguard competition in the long term;

(e) where appropriate, any relevant intellectual property rights; and

(f) the provision of pan-European services.

In principle, the MCA believes that agreements on any type of access should be reached following commercial negotiations between the parties. However, as stated above, on the basis of the SMP position enjoyed in the market, GO has an incentive to refuse to allow competitors to purchase wholesale call origination services. Mandating wholesale access is therefore deemed a justified and proportionate remedy to increase competition at retail level.

Primarily, GO should retain its existing access obligations and not withdraw access to facilities already granted without prior authorisation in writing by the MCA. In particular GO should continue to provide CS and CPS services to existing operators in accordance with Regulation 39 of the ESNCR . Moreover, GO should negotiate in good faith with any undertakings making new requests for such access. GO should also interconnect its network or network facilities with undertakings making reasonable requests.

In order to ensure that other operators will be able to offer end-to end or new products at retail level, the MCA concludes that it is essential that GO be obliged to continue to provide access to its wholesale line rental product in accordance with Regulation 21(2) of the ECNSR. Through the WLR product CS and CPS operators are able to offer a fully fledged replica of the incumbent's retail call service. It is widely acknowledged that the success of a CS/CPS services greatly impinges on the ability of the service provider to provide the end-user with a single bill for all retail call services. The MCA therefore maintains that the WLR is a necessary associated service to CS and CPS services and should therefore be provided by GO. As with the obligation of CS and CPS, GO should negotiate in good faith with any undertakings making new requests for WLR access.

The MCA further considers the availability of access to GO's technical interfaces, protocols or other key technologies that are indispensable for the provision of the services by other undertakings necessary for the creation of a truly competitive environment. Hence, GO shall be obliged to provide access in terms of paragraph (e) of Regulation 21(2) of the ECNSR.

Likewise, the provision by GO of access to operational support systems or similar software systems necessary to ensure fair competition in the provision of services is deemed necessary by the MCA. In addition, GO is required to provide other undertakings with services needed to ensure interoperability of end-to-end services to users.

In order for the above access obligations to be effective, GO must provide these services based on terms and conditions which are fair, reasonable and timely and which do not differ from those provided to its internal downstream provider. Moreover, access to the wholesale call origination services should be provided on an unbundled basis.

In all cases where access is to be provided upon a reasonable request being made, and the reasonableness of such request is disputed, the MCA will itself determine whether the request is truly reasonable or otherwise.

Whilst ensuring that no obligations are imposed unduly on any undertaking, the MCA, through its intervention aims at ensuring that no access is withheld or withdrawn unfairly.

The MCA believes that the obligation of access on its own is not sufficient to effectively regulate potential problems that may arise in this market. Consequently, the access obligation is to be supplemented with the obligation of transparency and in particular the publication of a reference offer for all the access services mentioned above. Furthermore, accompanying obligations of price control and cost accounting are deemed necessary.

4.4.2 Transparency

Regulation 18 of the ECNSR authorises the MCA to impose transparency obligations on undertakings holding significant market power in relation to interconnection and, or access, by requiring such undertakings to make public specified information, such as accounting information, technical specifications, network characteristics, terms and conditions for supply and use, as well as prices. The primary function of transparency obligations is to make other remedies, in particular access and non-discrimination, more effective.

The MCA believes that it is proportionate and justified to impose a transparency obligation on GO to ensure that it delivers services of quality to other operators as it provides to its own retail provider. The imposition of such remedy ensures that alternative operators have sufficient information and clear processes to which they would not otherwise have access. This would assist their entry into the market and directly targets the nature of such problems.

Regulation 18 further state that, where an operator with SMP has obligations of non-discrimination, the MCA may require it to publish a reference offer which shall be sufficiently unbundled to ensure that undertakings are not required to pay for facilities which are not necessary for the services requested, giving a description of the relevant offerings broken down into components according to market needs, and the associated terms and conditions, including prices. In such instances, the Authority is able to impose changes to reference offers to give effect to the obligations imposed under the Act.

At present GO is publishing call origination pricing as part of its Reference Interconnection Offer (RIO). The MCA believes that GO should to continue publishing reference offers related to all access products mention previously under the access obligation. Such offers are to be sufficiently unbundled, include pricing, terms and conditions and service level agreements as directed by the MCA.

In order to better overcome the competition problems discussed above, GO should continue to provide and publish appropriate manuals, order forms and processes for services. The publication of other information may be requested by the MCA from time to time.

The MCA reserves the right to specify the precise information to be made available, the level of detail required and the manner of publication of this information. The MCA believes that the imposition of transparency obligation ensures that a) services are not provided on a discriminatory basis; b) helps avoid any possible disputes, and c) accelerate negotiations between existing and potential operators. This obligation makes the access requirements more effective and makes it easier for the Authority to ascertain whether non-discrimination obligations are being met. The MCA believes that the requirements outlined are not excessively burdensome and will promote sustainable competition in the market.

4.4.3 Non-discrimination

A potential competition problem highlighted above is that an undertaking enjoying, individually or collectively, a position of SMP in a market, may have an incentive to provide wholesale services on terms and conditions that discriminate in favour of a particular undertaking in such manner as to have a detrimental effect on competition. It is the MCA's view that such an undertaking will have an incentive to give internal downstream operations a lower price than the ones offered to competitors and thus, be able to subject competitors to a margin squeeze. Undoubtedly, such a competition problem may have an adverse impact on competition in the downstream markets.

Besides price-related competition problems, an SMP operator may also resort to non-price anti-competitive tactics such as the withholding of information, delaying tactics, undue requirements, low or discriminatory quality, strategic design of products, and discriminatory use of information. These conditions will disadvantage competing providers and ultimately end-users.

In this light, the MCA is of the view that it is necessary that the access obligation delineated above be supplemented with a non-discrimination obligation. The MCA believes that such a non-discrimination obligation shall counteract price parameters as well as target non-price parameters.

In accordance with Regulation 19 of the ECNSR, GO, as an SMP vertically integrated provider would be obliged to:

a) apply equivalent conditions in equivalent circumstances to other undertakings providing equivalent services, and

b) provide services and information to others under the same conditions and of the same quality as it provides for its own services, or those of its subsidiaries or partners.

The obligation of non-discrimination, as specified in accordance with Regulation 19, will provide the same ability to alternative operators to obtain wholesale call origination and associated wholesale services at the same price and conditions which would apply to GO's downstream provider. Moreover, the information and services related to any wholesale services provided to alternative operators should be similar to those provided to its internal retail service provider.

The MCA also believes it is important that information gained by GO as a result of its provision of services to another operator is not used by its downstream activities in any manner to obtain any unfair advantage.

4.4.4 Price Control and Cost Accounting

Regulation 22 of the ECNSR authorises the imposition of obligations relating to cost recovery and price controls, including obligations for cost orientation of prices and obligations concerning cost accounting systems, for the provision of specific types of interconnection and, or access. Such intervention is in itself deemed instrumental in supporting competition in the retail market for the benefit of end-users, whilst at the same time supporting the obligations of non-discrimination and transparency at a wholesale level.

Where competition does not provide pricing constraints, it is necessary to prevent excessive pricing by means of regulation. Without some intervention in pricing, dominant providers are likely to charge excessive prices in order to maximise both their profits and the costs of competing providers. Higher wholesale charges are likely to translate in terms of higher retail prices and alternative service providers being less able to compete in the retail market at the detriment of end-users.

One of the competition problems identified before is that GO is vertically integrated SMP operator which can engage into excessive wholesale charging, to evict competition at retail level. The MCA is therefore of the opinion that GO needs to comply with the obligations of price control and cost accounting.

In mandating these obligations the MCA is obliged to ensure that any cost recovery mechanism or pricing methodology that is mandated serves to promote efficiency and sustainable competition as well as maximise consumer benefits.

Price Control

In view of the risk of excessive pricing being applied by GO in the wholesale call origination market, the MCA is of the opinion that the pricing for wholesale call origination needs to be regulated. Following the market analysis decision of the Wholesale call origination market published 2006[5], the MCA had imposed cost orientation on GO for the purpose of establishing wholesale call origination rate. By mandating that access to wholesale call origination services provided by GO are cost oriented, the MCA believes that it would be in a position to ensure fair and efficient access to GO's wholesale call origination services.

With respect to CS and CPS services, the MCA had issued a decision in 2004[6] (with subsequently revisions and additions of new services to be offered under CS/CPS obligations), on the way it should be implemented. The CS/CPS price control measure adopted by the MCA was that of cost-orientation, with the rate being obtained from a

[5] http://www.mca.org.mt/infocentre/openarticle.asp?id=880&pref=1

[6] http://www.mca.org.mt/infocentre/openarticle.asp?id=434&pref=1

cost model. In 2007, the MCA published a decision on the implementation of WLR where the price control method adopted was that of retail minus[7].

The MCA believes that in order to safeguard competition GO ought to continue to apply these price control measures for the provision of wholesale access services. The MCA reserves the right to change and or amend the price control measures adopted following appropriate consultation with interested stakeholders. GO is also to provide to the MCA all the necessary information, and in the level of detail as established by the MCA, for it to establish both the pricing for all wholesale call origination and associated services, as well as to determine an adequate relationship with retail prices.

Prior to the imposition of obligations of price control and cost accounting, the MCA has taken into account the investment made by the operator and will allow the operator a reasonable rate of return on adequate capital employed, taking into account the risks involved.

Cost Accounting

The MCA concluded that wholesale call origination and associated services, should be governed by virtue the provisions set in Regulation 22. The Authority therefore believes that a cost accounting system will be necessary to support such an obligation and is therefore imposing this as a further obligation on GO.

The MCA is of the view that if it does not impose such an obligation, GO could maintain some or all of its prices at an excessively high level, or impose a margin squeeze so as to have adverse consequences on competing operators and end-users. If the MCA were to relax this obligation, it would not have the necessary means of ensuring price controls in the market and prevent potential market failures.

At present GO is already maintaining such a system following the market analysis decision published in 2006[8]. The MCA therefore considers that GO should maintain the existing level of cost accounting system in accordance with the existing guidelines published by the MCA[9].

Such cost accounting system will provide the MCA with detailed information regarding GO's service costs and ensure that fair, objective and transparent methodologies are followed by the operator in allocating costs to the regulated services. Information from such a system will be used by the MCA to complement the application of other regulatory measures, such as transparency and non-discrimination.

4.4.5 Accounting Separation

In order to further strengthen the obligations of transparency and non-discrimination, the MCA considers it necessary to apply the complementary obligation of accounting separation on GO.

Accounting separation is instrumental in ensuring that the undertaking with SMP is not price discriminating between its retail arm and its competitors when providing access and origination at a wholesale level. By evidencing the wholesale and internal transfer prices

[7] http://www.mca.org.mt/infocentre/openarticle.asp?id=1070&pref=1

[8] http://www.mca.org.mt/infocentre/openarticle.asp?id=880&pref=1

[9] Implementation of Cost Based Accounting Systems for the Telecommunications Sector - Report on Consultation and Decision - July 2002

of the products and services of the undertaking with SMP, accounting separation ensures that the prices charged by the SMP operator are non-discriminatory.

The obligation of accounting separation is also important in the disclosure of possible market failures such as cross-subsidisation and the application of margin squeeze by an undertaking with SMP.

In view of the above and of the fact that the MCA is herein imposing the obligations of non-discrimination and transparency on GO, the MCA proposes that the imposition of an accounting separation obligation on GO is appropriate. Currently, GO is subject to the accounting separation obligation described in the MCA decision on Accounting Separation[10]. This level of obligation shall be maintained until further consultation is deemed necessary.

4.5 Monitoring Market Developments

The MCA believes that it important to keep vigilant on any market developments following this review. This would ensure that the obligations on the SMP operator identified earlier on, would be justified throughout the duration of this market review. If the MCA deems it necessary or appropriate a new market review would be undertaken at any time in response to significant changing market conditions. The MCA will also monitor the effectiveness of the regulatory obligations imposed such that alternative operators are able to compete in the retail market.

[10] 'Accounting Separation and Publication of Financial Information for Telecommunications Operators - Report on Consultation and Decision of October 2002' as amended - see http://www.mca.org.mt/library/show.asp?id=323&lc=1

Appendix 1

MINISTERU TAL-FINANZI, L-EKONOMIJA
U INVESTIMENT

MALTA

MINISTRY OF FINANCE, THE ECONOMY
AND INVESTMENT

DIVIŻJONI TAL-KONSUMATUR
U TAL-KOMPETIZZJONI

CONSUMER AND COMPETITION
DIVISION

Uffiċċju tad-Direttur Ġenerali

Office of the Director General

29 SEP 2009
RECEIVED

25 September 2009

The Chairman
Malta Communications Authority
Valletta Waterfront
Pinto Wharf
Floriana

Dear Chairman,

The Office for Fair Competition (OFC) has been asked to provide its opinion in respect of the Malta Communications Authority's (MCA) consultation documents dated 27 May 2009 concerning the market analysis on:

1. Wholesale call origination services provided over fixed electronic communications networks; and

2. Retail access to the public telephone network at a fixed location.

The OFC contends that the market assessment as conducted by the MCA follows standards that are in line with best practices normally used when defining relevant markets in competition analysis. The OFC considers that it is reasonable to accept for the period under review the MCA's findings on the said markets as presented in the consultation documents. However, given the nature of these markets, it would be appropriate to constantly monitor market developments.

We would like to point out that our views are being submitted in the context of the specific provisions of the SMP guidelines relating to the relationship between markets defined for the purpose of ex-ante regulation vis-à-vis competition law enforcement. The OFC reserves the right to re-examine any or all of the issues underlying these MCA recommendations in the light of facts and evidence that may arise in specific cases before it.

Yours sincerely,

Dr Mireille Vella
Director General

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