REGULATION TO IDENTIFY THE RELEVANT MARKETS IN THE ELECTRONIC COMMUNICATIONS SECTOR

PART 1

1. INTRODUCTION

1.1. Regulation Objective

The Regulation to identify the relevant markets in the electronic communications sector, establishes those products or services markets whose characteristics can justify why the National Regulatory Authority for Communications, hereinafter called ANRC, can impose specific obligations to the electronic communications services or networks providers with a significant market power.

Determining the market implies identifying and defining the competition borders among the electronic communications services providers. Defining the relevant market is achieved by systematically identifying the competitive constraints, which the electronic services and networks providers have to face. The main objective in defining the products/services market and the geographic market is identifying those real or potential competitors, capable to impose constraints on the behavior of other competitors and prevent their independent behavior, through an efficient competitive pressure.

Defining the relevant market allows the market share calculation of the electronic communications services providers. The information related to the market share is essential to the market analysis, in order to establish the electronic communication services and network providers with significant market power. The market analysis will be done based on the "Regulations to conduct market analysis and determine the SMP", which will be applied by ANRC in strong connection with the present regulation.

The Regulation to identify the relevant markets in the electronic communications sector establishes the criteria and instruments to be used by ANRC in order to determine the relevant markets in the electronic communications sector, whose characteristics can justify why ANRC can impose certain obligations to the electronic communications services and network providers with significant market power.

1.2. The Legal Framework

- E.G.O. no. 79/2002, regarding the general regulatory framework of communications in Romania;
- G.O. no. 34/2002 regarding the access to the public electronic communications networks and the corresponding infrastructure, and their interconnecting, approved with modifications and additions by Law no. 527/2002;
- Competition Law no. 21/1996.

2. CRITERIA TO DEFINE THE RELEVANT MARKETS

ANRC may impose *ex ante* obligations to the SMP operators, at the level of the wholesale markets, based on the G.O. 34/2002 regarding the access to the public electronic communications network and the corresponding infrastructure, and their interconnecting. Law no. 527/2002 approved this G.O. with modifications and additions. The retail markets, previously mentioned, will be examined only to define the wholesale markets, nondiscriminatory and irrespective of the technology, network or infrastructure used to provide electronic communications services.

In order to serve the users, the *ex ante* regulation has as a goal the prevention of potential issues among the new entrants on the market, in getting access to the existing networks of other operators and in negotiating interconnection charges for a competitive supply of electronic communications services.

A relevant market comprises a product or a group of products and the geographic area were they are produced and sold. The relevant market has two components: the product/service market and the geographic market.

2.1. Criteria to Define the Relevant Products / Services Market

The relevant products/services market is that products/services market, considered by the users to be interchangeable or substitutable, due to their features, price and the intended usage.

The definition criteria of the relevant product market apply also to the relevant service market. To simplify the terminology, the "relevant product market" notion will be used hereinafter.

2.1.1. Demand Substitution

ANRC will use the demand substitution criterion to determine those products or range of products that the consumer could easily switch in case of a relative price increase.

In order to determine the existence of demand substitution, ANRC will examine the consumer behavior related to a historic price fluctuation of the potential competitive products. It will also examine the change in the consumer preferences towards other products in response to a product or group of products price increase.

Identification of the products considered to be substitutable by the consumers will be done based on the "relevant market test" (hypothetical monopolistic test). This experiment involves a small, significant and non-transitory price increase. Through a small but significant change of the price it is understood a modification of the price by 5-10%.

Starting from a product or group of products, other products will be included in, or excluded from, the definition of the product market, depending on how much they influence, on a short term, the price of the products existing on the market.

If, as a result of a small, significant and non-transitory price increase on the market, the consumers will switch to the available substitutable products, or the providers from other markets will enter the relevant market, those substitutable products will be included on the relevant market.

2.1.2 Supply Substitution

ANRC will use the supply substitution criterion to establish the existence of the electronic communications services and networks providers that will decide to enter a market, in a reasonable period of time and without significant costs, if a significant price increase occurs on the market.

In defining the market, the substitution offer is taken into account when its effects are equivalent to those of the substitution demand in what concerns the influence and the direct action in setting up the market price. This means that the providers can sell those products on the relevant market, immediately and without assuming any supplementary, significant costs or risks, in case of a small, significant and non-transitory increase of the price on the market.

The relevant product market will comprise all the products that are substitutable from the demand/supply point of view, and the current total sum of these products will determine the total value or the market volume.

When the supply substitution involves significant modifications of the existing network facilities, important supplementary investments, or more time, this supply will not be included into the relevant market.

2.1.3. The Hypothetical Monopolistic Test

The "hypothetical monopolistic test" is an experimental instrument used to identify the demand and supply substitution in order to examine the price constraints over a network and electronic communications services provider. It implies an analysis of whether the joint profits of the providers will increase, once they have raised their prices for products and services by 5-10%. The analyzed market is a relevant market, separate and distinct when their joint profits increase.

From the point of view of the demand, the relevant market test determines if there are substitutable products available to the consumer, in case of a small but significant price increase, without any additional efforts or costs on their part. If the consumers can substitute the existent products with other products, in case of a 10% price increase, these other products will be included on the relevant market. The test is repeated for the new group of products until no more items can be included on the market.

To evaluate supply and demand substitution, the following factors have to be considered:

- The way in which clients or providers reacted to the previous price modifications
- The extent to which the consumers would assume the costs in case they change one product with another and the time they need to make this change;

- The extent to which the providers take their business decisions by taking into account the consumers’ reaction to the prices’ raise.

If the market price level is too high, as a result of an inefficient product market competition, the demand substitution evaluation, starting from this price level, can lead to the introduction, on the relevant market, of some products that would not be substitutable, if the initial prices had been established on competitive principles.

If the market price level is too low, as a result of the existence of some not competitive regulations or practices on the product market, the demand substitution evaluation, starting from this price level, can lead to the exclusion, from the relevant market, of some products that would be substitutable if the initial price had been established on competitive principles. In such cases, ANRC will decide if the demand substitution criteria are relevant in defining the relevant market.

The test is applied similarly in the supply case, considering the reaction of those operators who do not offer, but have the possibility to offer, similar products in a short period of time and without assuming any relevant costs or risks.

2.1.4. Other Criteria used in Defining the Relevant Markets

The analysis to define the relevant market is done in order to evaluate the necessity of imposing *ex ante* regulatory measures and starts from a comprehensive evaluation of the structure and functioning of the market in the future.

A. Market Entry Barriers

This criterion establishes whether a market has high-level entry barriers. The presence of such high-level entry barriers, although useful, is not necessarily enough to guarantee identification of a new market for the objectives of the present regulation. Given the dynamic character of the electronic communications markets, the chances for a market to become competitive must also be taken into account despite high-level entry barriers on the market.

According to this criterion, there are two types of barriers that impede access on the market and competition evolvement: structural barriers and legal ones (or regulatory barriers).

Structural Barriers

We have a structural entry barrier on the market when the technological level, associated infrastructure costs and demand level can establish discriminatory conditions among the incumbents and the new entrants. These discriminatory conditions will lead to the impediment or delay of the market entry for the latter.

High entry structural barriers can exist on the market, when the market is characterized by substantial scale, scope and density economies, and high sunk costs.

The scale economies appear when the total average costs of an operator decrease while the production volume and/or sold services increase. They are influenced by technological factors and result from the decrease of the fixed prices per unit of product or services, because of the increased sale volume.

The scope economies evolve as a result of the cost advantages of an operator who provides two or more linked products, as opposed to the operators that provide only one product/service. The scope economies exist together with, or separate from, the scale economies.

The density economies evolve as a result of the cost advantages of an operator who benefits from the high density of users.

The sunk costs are those fixed costs that cannot be recovered or avoided even when a total production failure occurs.

Legal or Regulatory Barriers

Legal market entry barriers do not link to the economic conditions. They evolve from legal measures that have a direct effect over the entry conditions and/or operators' positions on the relevant market.

A significant legal or regulatory barrier also exists when the entry on a certain market is considered not viable because of the existing regulatory conditions, which are being estimated to last for a long time.

B. Market Dynamics

The second criterion determines whether or not there are market characteristics to lead to an efficient market competition, despite the existence of some high-level entry barriers, without implying any *ex-ante* regulations.

The market entry barriers can be less relevant on those markets characterized by a fast technical progress. On such markets, the competitive constraints appear often from the innovative pressure received from the competitors that are not on the market at that moment. On the strongly innovation influenced markets, there is a potential long- term competition among operators considered not to be competitors on a "static" market.

C. Sufficiency of the Competition Law

In identifying a market that will justify possible *ex ante* regulatory measures, the extent to which the competition law can lead to an efficient competition in the absence of *ex ante* regulatory measures, should be considered, in addition to the first two criteria.

The *ex ante* regulatory measures are being added to the competition legislation when the experience gained on the national and international markets proves that the competition legislation could not stop market failure.

D. Exclusive Rights

The exclusive rights for the provision of certain electronic communications services involve an evaluation of the markets of these services and an identification of the corresponding wholesale markets as relevant for *ex ante* regulatory purposes.

The extent to which ANRC intervention on the market is justified depends on the presence of some historic or present exclusive rights, the persistence of some high entry barrier, the market dynamics and an efficient application of the competition law.

If based on a market analysis ANRC establishes that on a relevant market there is an efficient competition, it will not apply any of the *ex ante* regulatory measures or it will withdraw them if these exist.

If based on a market analysis ANRC establishes that on that relevant market there is no efficient competition, ANRC will identify the electronic communications networks or services providers with significant market power, and will impose to them, correspondingly, one or more *ex ante* regulatory measures, or it will maintain or modify these measures, there where they already exist.

2.2. Geographic Market

The relevant geographic market covers the area where the economic agents involved in providing electronic communication services and networks, are located, where the competition conditions are homogeneous enough, and that can be differentiated from neighbor geographic areas due to different competitive conditions.

To define the geographic area it is not necessary for perfectly homogeneous competitive conditions to exist among operators. It is sufficient that these are similar or homogeneous enough and only those areas where the competition conditions are heterogeneous will be excluded from the geographic market.

To define the geographic limits of the product, it is necessary to identify the extent to which the closeness among potential operators can impose competitive constraints.

The process to define the geographic market is similar to that of defining the product market, starting from the evaluation of the demand and supply substitution as an effect of a relative price increase.

In relation to the demand substitution, ANRC will evaluate the consumer preferences and the buying behavior within the geographic area.

With concern to the supply substitution, ANRC will evaluate the extent to which the operators that do not belong to the considered geographic market can decide to access it soon.