



**BEREC Opinion on
Phase II investigation
pursuant to Article 7 of Directive 2002/21/EC as amended by Directive 2009/140/EC:**

**Case FR/2014/1670
Wholesale SMS termination on individual mobile networks in France**

29 December 2014

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1. EXECUTIVE SUMMARY

On 28 October 2014, the Commission registered a notification by the French Regulatory Authority, Autorité de Régulation des Communications Electroniques et des Postes (ARCEP), concerning the wholesale markets for (i) call termination on individual public telephone networks provided at a fixed location, (ii) voice call termination on individual mobile networks, and (iii) for SMS termination in Metropolitan France and overseas territories.

In the notified draft measure, ARCEP defines a separate SMS termination market for the provision of termination services in each mobile operator's network. All mobile operators are proposed to be designated with SMP on their respective market. The obligations of access, transparency, non-discrimination and price control will be imposed on all SMP operators active on the territories covered by the present analysis.

On 28 November 2014, the Commission sent a serious doubts letter opening a Phase II investigation pursuant to Article 7 of Directive 2002/21/EC as amended by Directive 2009/140/EC. The Commission's doubts concern:

- The need to analyse competitive constraints on a forward looking basis;
- A potentially broader market for SMS termination in France;
- The reliability of the SMP assessment.

On the basis of the analysis set out in this Opinion, BEREC considers that the Commission's serious doubts are, overall, partially justified.

BEREC suggests that ARCEP should integrate the additional supportive evidence that was presented to both the Commission and BEREC, into the final decision.

2. INTRODUCTION

On 28 October 2014, the Commission registered a notification from the French Regulatory Authority, ARCEP, concerning the wholesale markets for (i) call termination on individual public telephone networks provided at a fixed location, (ii) voice call termination on individual mobile networks, and (iii) for SMS termination in Metropolitan France and overseas territories.

On 6 November 2014, a request for information (RFI) was sent to ARCEP, and a response was received on 12 November 2014. An additional request was sent to ARCEP on 13 November 2014 and a response was received on 17 November 2014.

The Commission initiated a Phase II investigation with respect to the market for SMS termination, pursuant to Article 7 of Directive 2002/21/EC as amended by Directive 2009/140/EC, with a serious doubts letter on 28 November 2014. In accordance with the BEREC rules of procedure, the Expert Working Group (EWG) was established immediately after that date with the mandate to prepare an independent BEREC opinion on the justification of the Commission's serious doubts on the case.

The EWG met on 9 December 2014 in The Hague. During the meeting ARCEP presented its answers to questions, which they received from the EWG on 8 December 2014, and shared additional information regarding their decision to regulate the SMS termination market. All of the information provided during the meeting by ARCEP was distributed to the EWG on 11 December 2014. The meeting of the EWG was based on the objective of sharing the understanding of the notified documents and reaching a clear conclusion on whether the Commission's serious doubts are justified. The EWG reached preliminary conclusions on these issues, by analysing the relevant documents and exchanging information with ARCEP.

A draft opinion was finalized on 17 December 2014 and a final opinion was presented and adopted by a majority of the BEREC Board of Regulators on 29 December 2014. This opinion is now issued by BEREC in accordance with Article 7(5) of the Framework Directive.

3. BACKGROUND

Previous notifications

The first review of the SMS termination market for mainland France dates back to 2006¹.

The second review of the wholesale markets for SMS termination services of mobile network operators (MNOs) in metropolitan France and the first review of markets for those services in the French overseas areas were notified to and assessed by the Commission under case number FR/2010/1094².

ARCEP defined a separate market for SMS termination services on each of the mobile networks. The proposed market definitions covered the provision of SMS termination provided for other mobile and fixed network operators, internet access providers and so called "aggregators" of SMS (for the termination of SMS Push services³). Since the SMS termination market was not covered by the 2007 Recommendation on relevant markets, ARCEP carried out the three criteria test and concluded that the test in question is met for all the markets concerned. ARCEP proposed to designate all MNOs as having SMP and to impose on them the full set of obligations. Moreover, ARCEP proposed to make the obligation to provide termination at regulated prices subject to a reciprocity clause, i.e. only operators offering the same tariff could claim the regulated tariff. The Commission invited ARCEP to closely monitor the delivery of content onto mobile devices which might, according to the Commission, lead ARCEP to no longer include SMS Push services in the relevant SMS termination market and to consider removing regulation. Concerning the non-conformity of the proposed reciprocity clause with the EU law, the Commission invited ARCEP not to impose the proposed reciprocity clause in the final measure.

¹ FR/2006/0413/D 204005.

² C(2010) 5067; C(2010) 5276.

³ SMS Push services are used by banks, distribution firms, music or games editors and other content providers who wish to send content SMS to mobile end-users. At retail level these editors of services („éditeurs de service”) buy SMS Push services directly from MNOs or use aggregators („aggrégateurs”) to convey these SMS messages to the MNOs' customers. At wholesale level MNOs offer distinct SMS Push termination services to aggregators or other operators.

Current notification and the Commission's serious doubts

Current notification

In the currently notified draft measure, ARCEP defines a separate SMS termination market for the provision of termination services in each mobile operator's network. Like in the previous notification ARCEP defines a wholesale market that includes both the wholesale termination services for SMS Push services and the wholesale termination services for interpersonal SMS.

ARCEP does not consider, at this stage, that SMS can be substituted by other messaging services, including MMS and instant messages (IM) or e-mails sent via *peer-to-peer* internet applications, allowing the communication between subscribers using the same applications and a device connected to the internet.

ARCEP carries out the three criteria test and concludes that the SMS termination markets warrant *ex ante* regulation. ARCEP explains that because of a structural monopoly of mobile operators on their respective networks, the first criterion (high barriers to entry) and the second criterion (no tendency towards effective competition) are met. Regarding the fulfilment of the second criterion, ARCEP does not identify at the retail level any substitutes for SMS termination services that are able to exercise competitive pressure on the relevant market during the envisaged regulatory period. Finally, ARCEP considers that competition law alone is insufficient to address market failures, and has to be complemented with *ex ante* regulation.

All mobile operators are proposed to be designated as having SMP on their respective market for SMS termination. ARCEP's findings are based on the assessment of the following criteria: market shares, barriers to entry and countervailing buying power (both at retail and wholesale level).

The obligations of access, transparency, non-discrimination and price control will be imposed on all SMP operators active in the territories covered by the present analysis – Metropolitan France, and overseas territories, respectively. In addition, the obligations of cost-accounting and accounting separation will be imposed on Orange, SFR, Bouygues Telecom, Free Mobile, SRR and Orange Caraïbe. Also, ARCEP proposes a differentiation of the price control remedy between interpersonal and Push SMS termination services.

Commission's serious doubts

The Commission considers that the notified draft measure concerning the wholesale market for SMS termination on individual mobile telephone networks in France falls within the scope of Article 7(4)(a) and 7(4)(b) of the Framework Directive.

The Commission has serious doubts as to whether the market definition and the market analysis proposed by ARCEP meet the requirements laid down in Article 15(3) and 16(4) of the Framework Directive and, accordingly, whether ARCEP's notification complies with the principles provided in Article 8 (2) a) and b) of the Framework Directive.

The Commission, therefore, expresses serious doubts as to the compatibility of the draft measures concerning the wholesale market for SMS termination on individual mobile networks in France with EU law for the following principal reasons:

- Need to analyse competitive constraints on a forward looking basis;

- Potentially broader market for SMS termination in France;
- Reliability of SMP assessment.

4. ASSESSMENT OF THE SERIOUS DOUBTS

On 28 November 2014, the Commission sent a serious doubts letter opening a Phase II investigation pursuant to Article 7 of Directive 2002/21/EC as amended by Directive 2009/140/EC. Commission's doubts concern compliance of ARCEP's draft measure with EU law, in particular with respect to Article 15(3) and Article 16(4) of the Framework Directive regarding the requirements for market definition and market analysis. The Commission considers that ARCEP did not provide sufficient evidence to support its findings that the SMS termination in France was defined/ analysed in accordance with competition law principles for the purpose of *ex ante* regulation.

1. Need to analyse competitive constraints on a forward looking basis

Concerns of the Commission

The Commission emphasizes that the SMS call termination market has never been listed in the Recommendation on Relevant Markets as a market susceptible to *ex ante* regulation. However, the Commission notes that NRAs may decide to regulate this market, taking into account the national circumstances, by taking utmost account of the Recommendation on Relevant Markets, which provides for a three criteria test to be followed when defining such a market. NRAs could do so, only if this is justified on a forward looking basis. The Commission considers that, when defining a relevant market in a forward looking perspective, ARCEP:

- has not appropriately addressed the tendency towards effective competition, by taking into account the impact of possible competitive constraints that could be exerted at retail level by alternative IM services sent via *peer-to-peer* internet applications;
- did not assess in detail the future evolution of IM in France (i.e. potential growth or decline) as compared to SMS services;
- did not consider the fact that the regulation of the SMS termination market and the resulting low retail SMS prices could lead to persistent overregulation impeding structural market developments, which would have taken place absent regulation in the market.

Views of ARCEP

ARCEP states that all three criteria (high and non-transitory barriers to entry, no tendency towards effective competition, insufficiency of competition law in resolving the identified competition failures) are met and therefore the SMS termination market in France is susceptible to *ex ante* regulation. The second criterion (no tendency towards effective competition), whose fulfilment was considered of concern by the Commission, is met because there are no substitutes for SMS services at the retail level that would be able to exercise competitive pressure on the relevant wholesale market during the relevant regulatory period. As for the SMS and IM substitutability, ARCEP states, in the response to the RFI, that the substitutability would remain partial because of the limited penetration of mobile internet services, the need to have a compatible terminal, e.g. smartphone, the need for payment of

an additional fee for having access to mobile internet services, the existing coverage, and absence of interoperability between different IM applications. Taking that into account, ARCEP concludes that SMS services are the most convenient form of communication for the end-users, while IM services are rather complements than substitutes for SMS services.

ARCEP also states that the continuing increase in SMS usage is an indication that the IM services do not provide sufficient competitive pressure. This conclusion is supported by the fact that the smartphone penetration in France was estimated at only 53% of the French population aged over 15 in the second quarter of 2014, while 51% of the capable mobile terminals (including smartphones) had access to mobile internet in the third quarter of 2014, i.e. lower compared to other EU countries.

During the meeting on 9 December 2014 in The Hague, ARCEP presented market forecasts regarding the development of IM in France, from two reference studies – one conducted by Analysys Mason and the other by Portio Research. Based on those reports, ARCEP concludes that although IM services are developing, SMS and IM will be more complementary services rather than substitutes at the retail level in France. The supporting arguments are (1) that the addressable “text conversation cases” by IM services will remain limited (<36% for most of the period); (2) there is no guarantee that the absence of interoperability of current IM services would be compensated either by an interoperable IM platform or by a generally used (dominant) OTT service; (3) restrictions due to data network low usage by the French consumers and (4) continuing high levels of SMS consumption.

ARCEP explains that the main objective of maintaining regulation is to preserve competitive dynamics achieved so far. Continuing the regulation of the SMS termination market would lead, on the one hand, to ensured stability of wholesale prices (which also affect retail offers) and, on the other, to ensured symmetry of termination tariffs between regulated operators and operators that have not been regulated so far. ARCEP stresses that the latter approach is supported by all operators. ARCEP argues that IM platforms are not threatened by the proposed regulation and will continue to develop. Quoting Portio Research: “Yet, alongside a vibrant SMS market, OTT messaging enjoying solid growth in France too [...] This is again attributed to the rapidly growing penetration of smartphones in the country and the strong culture of P2P messaging”⁴.

BEREC's Assessment

ARCEP's contention is that IM services and SMS are complements. However, in the Phase I procedure ARCEP has not put forward any evidence that suggests they are complements. However, the key question in this procedure is whether IM and SMS services are substitutes.

BEREC agrees with the Commission to the extent that potential substitutes such as IM services from OTT providers should be considered in the market analysis for wholesale SMS termination at the retail level. It is due to the fact that wholesale termination services are by definition structural monopolies, that focusing on the analysis at wholesale level alone could lead to a situation with persistent overregulation.

⁴ Portio Research, 2014, Mobile messaging futures 2014-2018, non-public study, <http://www.portioresearch.com/en/messaging-reports/mobile-messaging-research/mobile-messaging-futures-2014-2018.aspx>

Considering that the demand for termination services is derived from the demand at retail level, these two levels are related. In this case, the higher the demand for IM services, the higher the competitive pressure on SMS services at the retail level. The competitive pressure on SMS services at the retail level coming from potential substitutes, i.e. IM services, that do not need wholesale termination as an input product, increases the elasticity of demand at the wholesale level hence resulting in a higher price pressure⁵. On the other hand, BEREC considers that even if the SMS termination rates are kept above cost level, it is still not clear whether this would have detrimental effects on retail SMS services. Therefore, if there is a sufficient competitive constraint at the retail level, operators would not be able to pass higher termination rates onto retail consumers.

Taking the above into account, BEREC is of the opinion that in order to fully consider the competitive dynamics in the SMS termination market, it is necessary to analyse the vertically associated retail market, as well. If there is a competitive constraint at the retail level, it is questionable whether it is justifiable to regulate the corresponding wholesale market on the grounds of *ex ante* regulation, as it is laid down in the Commission's Recommendation on relevant markets susceptible to *ex ante* regulation.

BEREC believes that the underlying question here is whether a sufficient number of customers are willing and in this case more importantly are able to switch services, in order to render a price increase unprofitable⁶. When analysing whether SMS services' users would be willing and able to switch to IM services, it must be taken into account that the transition to IM services requires certain additional elements, i.e. compatible terminal (e.g. smartphone), access to mobile internet, having the appropriate application installed on a compatible terminal, etc. These additional elements can induce significantly higher costs than the 5% to 10% price increase for the provision of SMS retail services.

As mentioned in their response to the Commission's RFI, ARCEP has commissioned a survey by Mediamétrie and a study by CREDOC. These studies give crucial elements for conducting a SSNIP⁷ or HM test⁸. However, ARCEP did not include such an analysis in their notified market review to support the draft decision.

In this respect, BEREC asked ARCEP to make available data about the development of mobile broadband and IM services in France. ARCEP provided the EWG with the studies and surveys on this matter.

According to ARCEP, in order to use an IM platform a customer needs a smartphone and a tariff plan with mobile data. The take-up of mobile broadband in France seems to be lower than in many other countries. According to the Digital Agenda Scoreboard⁹ most recent data available, at the end of 2013 the take-up of mobile broadband in France was 48%, significantly

⁵ However, even in countries with a very high usage of IM services operators seem not to have reduced their termination charges. This might be connected to the communication pattern of SMS services. If a customer sends an SMS, he or she usually receives a reply message. Because of that, traffic tends to be relatively symmetric between interconnection partners, with the consequence that retail price cuts do not necessarily lead to significant net payments.

⁶ One crucial question is how many customers have to switch to IM services to make a 5-10% price increase unprofitable. A critical loss analysis could produce some guiding benchmarks.

⁷ Small but significant non-transitory increase in price test.

⁸ Hypothetical monopolist test.

⁹ The Digital Agenda Scorecard defines mobile broadband as internet access by 3G or higher speed technologies and the unit of reference is SIM/USIM cards – mobile broadband data therefore includes M2M subscriptions. Mobile broadband penetration figures excluding M2M subscriptions will be lower.

lower than in the United Kingdom (89%), Spain (73%) and Italy (66%). Thus, less than 50% of the customers had a tariff plan with data subscription in France in late 2013. The cheapest tariff plans with mobile data traffic included cost around 9.5 €/month (for data traffic up to 200 MB) and 19.99 €/month (for data traffic up to 3 GB). These tariffs are significantly higher than tariff plans which include voice traffic and unlimited number of SMSs (2 to 4.99 €/month). Therefore, a customer that has no data plan subscription must bear significant additional costs in order to use an IM platform, besides the costs incurred with the acquisition of a smartphone, if he or she does not have one.

The use of IM services in France is much lower than in many other countries. Whereas in Spain, Italy and Germany respectively, 99%, 93% and 91% of the *Iphone* users made use of *Whatsapp* IM service in June 2013, only 17% of the *Iphone* users in France used it.¹⁰ ARCEP argues that, for the time being, due to the low take-up of IM applications and due to club effects, less than 10% of messages that are sent between two parties could be sent via an IM platform.¹¹ Furthermore, even if the remaining number of the customers who use SMSs is fairly high, substitution potential being present, not all of these customers would really switch, as a reaction of a price increase. The limited switching from SMS services to IM services can also arise due to the fact that price sensitive customers tend to use attractive tariff plans for voice and SMS services that do not include data services. Moreover, ARCEP argues that because of handset prices and extra cost for data packages (twice as expensive as offers without data), it is unlikely that customers would turn to IM services or applications as a consequence of 5–10% price increase of SMS services. Thus, under the assumption that an end-user neither owns a smartphone, nor has a data subscription plan, any 5–10% price increase in the provision of SMS services will be profitable and, hence, not resulting in substitution for the services considered. As a result of the low usage of IM services, SMS consumption per capita in France is much higher than in many other European countries and, contrary to the general trend, it is not decreasing.

When it comes to the future evolution of IM services in France, BEREC would like to highlight the results of the research concerning the substitution possibilities between IM services and SMS services in the time frame of the market review, presented by ARCEP during the meeting on 9 December 2014. ARCEP provided a comparison between the share of French consumers who had the possibility to substitute SMS services for IM services in 2014 and an optimistic forecast for the same indicator in 2017. Accordingly, they show that only 31% of the 76.6 million mobile phone users had, in 2014, an IM application installed on their terminal, compared with the optimistic forecast of 60% of the mobile phone users in 2017. In turn, this implies that currently 69% of the mobile phone users are either not addressable (basic phone users) or not addressed (smartphone users who do not have any kind of IM application installed on their terminal). The relevant figure forecasted in 2017 would be 40% for users who are either not addressable or not addressed. If the aforementioned figures were to be considered relative to/ in correspondence with the number of SMS text messages potentially sent in each case, 90% of the current text conversation cases are either not addressable or not addressed, while the corresponding forecasted figure for 2017 stands at 64%. Consequently, the maximum share of text messages that could potentially be substituted by IM services could increase from the current share of 10% to 36% in 2017. However, ARCEP stated in the meeting that club effects

¹⁰ Source: Onavo Study.

¹¹ As IM services are not interoperable the receiver and the sender need the same platform (to be in the same club). Therefore, an even smaller fraction of users can use an IM service.

due to a lack of interoperability between IM platforms further reduce the share of text conversation messages that can be sent via IM platforms.

Considering the elaborate and extensive answers ARCEP gave to the questions from the EWG, BEREC is of the opinion that ARCEP conducted an analysis regarding the forward looking perspective of the evolution of the IM services. However, ARCEP neither did include this analysis in the notified draft measure, nor did share the complete analysis with the Commission during the Phase I procedure.

BEREC highlights that the low SMS prices are not, in themselves, a limiting factor which prevents consumers from acquiring a smartphone or mobile internet access services, or from using IM services accordingly. It is BEREC's opinion that due to the enhanced functionalities of smartphones, consumers nowadays do not buy them solely for the purpose of traditional communication (i.e. voice and messaging). According to ARCEP's forecasts, it can be seen that despite SMS termination market regulation, the usage of IM services could increase significantly, i.e. 40% to 60% of mobile telephony users will not only have a smartphone but an application for IM, as well. This also supports the fact that SMS services prices, which might be derived from SMS termination price, do not limit the development of IM services.

To conclude, BEREC believes that the Commission's serious doubt, as far as the need to analyse the competitive constraints on a forward looking perspective and pressures from IM services in the vertically associated retail market, is partially justified. BEREC is of the opinion that ARCEP did conduct the required analyses but should have more elaborately presented their findings during the Phase I procedure, and preferably in the notified draft decision.

According to BEREC, the data provided by ARCEP, does not indicate that the regulation initiated in 2006 impedes structural market developments in the sense that it prevents alternative messaging services from developing and exercising competitive constraints on SMS termination. BEREC therefore does not agree with this part of the Commission's serious doubt.

Due to the fact that ARCEP provided the aforementioned information to BEREC and in a later stage to the Commission, BEREC suggests that ARCEP should also incorporate the analysis into the final decision.

2. Potentially broader market for SMS termination in France

Concerns of the Commission

The Commission is concerned with the fact that ARCEP did not carry out a SSNIP test in order to assess the impact of a small but significant non-transitory increase in SMS prices on the market, in particular with respect to the expected behaviour of consumers potentially switching to IM services, at the market delineation stage. In this respect, it notes that ARCEP approached the potential switching towards IM services at retail level under the Greenfield approach just in the SMP designation section (section 3.4.1), in the context of indirect countervailing buyer power. Also, ARCEP seemed not to assess in detail the evolution of IM services in France, by, for example, analysing the expected trend regarding IM services compared with the SMS services' evolution. Thus, ARCEP could have possibly defined a broader market, if it had

considered properly the possible constraints deriving from IM services sent via peer-to-peer applications.

Another point that the Commission raises is the fact that, while ARCEP's argumentation seemed to imply different market dynamics for interpersonal SMS and Push SMS services (particularly referring to the possibilities of interchangeability between Push SMS services and IM services, respectively for interpersonal SMSs and IM services), this was not further analysed by the French regulator.

To conclude, the Commission's second serious doubt questions the correct delineation of the market for SMS termination in France, given the lack of robust analysis of competitive constraints stemming from IM services, different technical characteristics of Push SMSs (as compared to interpersonal SMSs), as well as the proposed differentiation of price remedies at wholesale level.

Views of ARCEP

In its notified draft measure, ARCEP relies extensively on the previous market analysis concerning the SMS termination services. In the context of the substitutability analysis, it stated that "it does not observe developments in the substitutability analysis in comparison with its previous market analysis". Therefore, it considers appropriate to briefly present the main arguments put forward in the previous measures, making a reference to the 2010 decisions for details.¹²

Regarding the substitutability analysis in the retail market¹³, in particular with respect to the possible substitution of SMS services with IM services, it considers that, in the time-frame of the market review, the interchangeability of the analysed services remains limited. As a consequence, ARCEP concludes that the IM services represent complements rather than substitutes for the SMS services.

With respect to the application of the SSNIP test at retail level¹⁴, in the view of correctly delineating the relevant product market boundaries, ARCEP considers that the test cannot be applied as such to the retail market for SMS services. Since, for post-paid users¹⁵, almost all the SMS services are being sold bundled with voice and data traffic¹⁶, a small but significant non-transitory increase in SMS tariffs would determine a rise in the price of the respective bundles. Also, besides this price increase, the French regulator accounts for the costs generated by the handsets, if a user decides to switch to IM services, when SMS services' price increases with 5-10%. ARCEP presents figure no. 1, which shows the evolution of the cumulated price paid by consumers for different offers, for a period of 2 years, taken into account the fact that the reference prices in France are between 20 € for a basic phone and 100 € for an entry-level smartphone. According to these figures, a customer that purchases a smartphone and a tariff plan with data in order to be able to use an IM platform would face cumulated extra cost of up to 440 € over 2 years (592 € minus 152 €) which is significantly higher than a 5–10% price increase of SMS services.

¹² For further reference, please see section 2.2.2 of the notified draft measure.

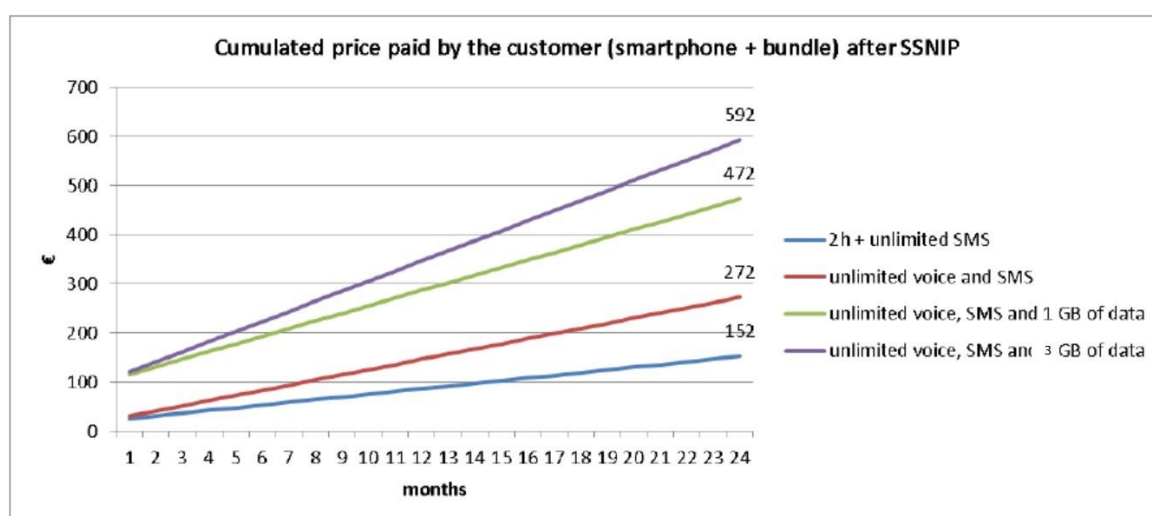
¹³ The presented reasoning is presented by ARCEP in section 2.2.2.3 e. of the notified draft measure.

¹⁴ The information presented in the current paragraph has been made available by ARCEP on the basis of the investigation conducted by BEREC.

¹⁵ 82% of the mobile users in France benefited from a post-paid plan in 2014.

¹⁶ In this case, subscriptions include an unlimited number of SMS messages.

Figure no. 1 – Estimation of the impact on consumers of an increase of the SMS tariff by 5–10%



The conclusion is that customers that do not have a tariff plan with data and a smartphone would not substitute usage of SMS services with the corresponding IM services as a response to the considered price increase.

Also, the currently notified draft review does not approach, in the context of market delineation or SMP designation, an analysis of the Push SMS services. However, in the conclusions' part regarding the susceptibility of termination markets for *ex ante* regulation (section 4.3), ARCEP provides a quote from the Explanatory Note to the Commission's Recommendation on relevant markets susceptible to *ex ante* regulation, saying that a SMS termination market – including interpersonal and Push SMS services – may be defined by the NRA based on the three criteria test.

In the answer to the RFI, ARCEP clarifies that, at a retail level, interpersonal SMS services and Push SMS services are not interchangeable due to the way in which they are marketed and their purpose – Push SMS services are designed for the delivery of content to the end-users and they are not part of end-users' retail offers. Furthermore, Push SMS services imply unilateral communication (the recipients of the messages are not expected and (or) have the possibility to reply), while interpersonal SMS services typically involve bilateral communication, i.e. a reply. However, given the specificities of termination services (the same wholesale market is upstream of all the SMS services provided in the retail market), termination services for Push SMS and for interpersonal SMS messages are part of the same relevant market.

BEREC's Assessment

BEREC firstly notes the importance of the relationship between the downstream retail market for SMS services and upstream wholesale market for SMS termination. In this respect, given that any market review aiming at regulating a wholesale market should start with the analysis of the competitive situation at retail level¹⁷, the related upstream wholesale market being

¹⁷ The Commission Recommendation - recital (7) states that “the starting point for the identification of wholesale markets susceptible to *ex ante* regulation is the analysis of corresponding retail markets.”

considered for regulation in case of identified competition failures in the retail market¹⁸, BEREC highlights that if ARCEP had concluded that SMS services and IM services are part of the same relevant retail market, wholesale regulation would not have been necessary. In the light of the above, BEREC considers that the Commission's concerns are also related to the definition of the retail market, in the view of the interdependence between them, and not solely to the definition of the wholesale market.

However, as it is widely recognised, termination services are the last replicable element in an electronic communications network, the provision of services in the retail market being dependent on the provision of termination services at wholesale level. Therefore, given that a sender needs to get in contact with a certain receiver, the sender's operator has no other option than buying termination services from the receiver's operator, be it termination for a fixed call, mobile call or SMS termination. In this view, there is no doubt that, should a termination market be found as susceptible to *ex ante* regulation, the relevant market will be defined as comprising the termination services on each operator's network. The relevant market for SMS termination can only be defined as comprising the SMS termination services on each individual mobile network, every operator offering the services holding significant market power in the correspondingly defined wholesale markets. BEREC refers in its opinion also to the definition of the retail market for SMS services. In this respect, after having thoroughly analysed the evidence provided by ARCEP in the course of the investigation, it notes that the French regulator seems to have conducted an in-depth analysis of the market data with respect to the potential substitution of the SMS services and IM services¹⁹, reaching its conclusion based on a proper assessment of the substitutability possibilities in France. However, BEREC is of the view that ARCEP should have presented the aforementioned evidence to the Commission in the course of the Phase I investigation.

With respect to the Commission's observation on the implied differences between the evolutions of interpersonal SMS services and Push SMS services that can be observed, BEREC notes that ARCEP confirms, in its answer to the RFI, that there are separate relevant retail markets for interpersonal SMS services and Push SMS services, implying that the French regulator accounts for the potential differences regarding these two services. However, at the wholesale level, the provision of SMS termination is the same irrespective of the type of SMS for which termination services need to be bought.

Taking all the above into consideration, also in corroboration with BEREC's conclusions regarding the first serious doubt raised by the Commission, BEREC does not share the Commission's serious doubt on the possibility of defining a broader market for SMS termination in France.

¹⁸ The Commission Recommendation – recital (10) states that “*If the retail market concerned is not effectively competitive from a forward looking perspective in the absence of ex ante regulation, the corresponding wholesale market(s) susceptible to ex ante regulation <...> should be assessed.*”

¹⁹ The relevant data provided by ARCEP refers to: the evolution of the monthly SMS consumption per customer in France, the fact that almost all of the retail postpaid offers currently available in France comprise an unlimited number of SMSs, the corroborated evolution of the average SMS consumption per month and average retail revenue per SMS, the fact that SMS services provide a viable alternative especially for the low income users, the take-up of IM services by French consumers shared across the most widespread applications in comparison with other European countries, the reasons put forward by the users of IM services, the prices for the cheapest mobile internet offer (significantly higher than the cheapest offer including voice and unlimited SMS), mobile broadband subscriptions as compared to other countries in Europe.

3. Reliability of the SMP assessment

Concerns of the Commission

The reliability of the SMP assessment was questioned as a consequence of the lack of conclusive evidence provided by ARCEP on the market delineation. The Commission is of the view that the SMP assessment may have been different if a broader market, that included IM services, would have been considered. Furthermore, the Commission is of the view that ARCEP, during the stage of the SMP assessment, should have anyhow thoroughly assessed the constraints coming from these services.

The Commission notes that the risk of abusive pricing in other Member States where SMS termination is not regulated does not seem to be observed. In view of low SMS termination rates in France (1 eurocent/SMS) relative to the average EU termination rate (2.5 eurocent/SMS), even if it does not dispose of evidence of whether the “what if competition” price would be closer to the EU average or to the regulated price-cap in France, the Commission is of the opinion that such risk may be overestimated in France.

Furthermore, the Commission does not agree with ARCEP’s assessment that the end-user welfare would be lowered if the market was deregulated. The Commission is of the view that ARCEP should have carried out a more detailed cost/benefit analysis to show that the benefit of having a larger choice of messaging services is outweighed by the disadvantage of decreasing SMS volumes. The Commission recognises that the acquisition of a smartphone for using alternative SMS applications represents an additional cost for consumers. However, it states that such cost is normally decreasing with smartphone penetration.

Therefore, the Commission has serious doubts that the proposed SMP assessment complies with Article 16 (4) of the Framework Directive and that it maximises end-user benefit in accordance with Article 8(2) of the mentioned Directive.

Views of ARCEP

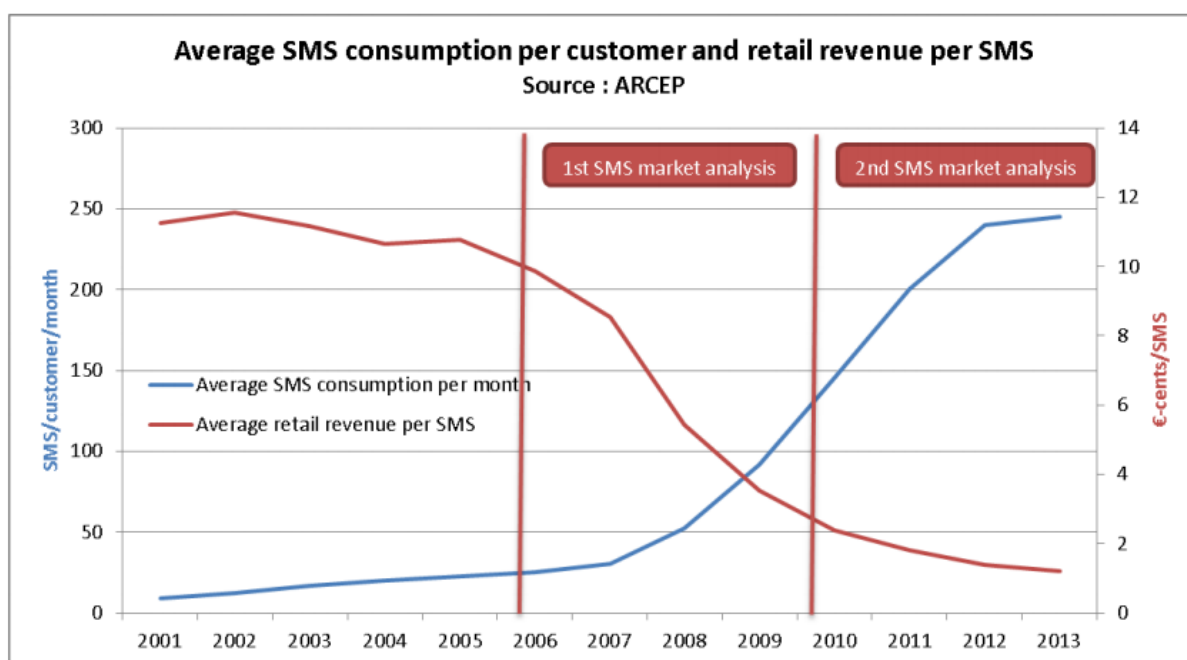
ARCEP states that, in its opinion, deregulating the market for SMS termination would lead to higher SMS termination rates. This opinion is based on the market developments prior to the notification of the current draft market analysis, specifically:

- In 2005, ARCEP received a complaint by one of the operators regarding potential harm stemming from the non-regulated SMS termination rates and, at the time, ARCEP decided to set a price-cap for SMS termination services in each MNO’s network.
- In the first market analysis (July 2006), ARCEP found two MNOs as holding SMP for the provision of SMS termination services in their networks and, correspondingly, regulated the SMS termination rates. The reasoning was that, at the time, the active operators in the market made it difficult for new entrants to be competitive.
- In its second round of market analysis, ARCEP introduced a price-cap for SMS termination of 1 eurocent/SMS. However, the non-regulated new entrants were setting higher termination rates than the regulated rate.

ARCEP therefore considers that SMS termination rates higher than the regulated ones prevent operators from competing on the retail market. Considering the time effectiveness of SMS

termination regulation, with the decreasing regulated SMS termination rates, operators were able to compete on volumes and, then, on prices – this made possible the inclusion of “unlimited SMS” offers in low-end plans in nearly all bundle offers. Thus, customers nowadays consider SMS services as free services. This point can also be demonstrated by the evolution of the SMS consumption per month, which is approximately at 250 SMS per SIM card per month, one of the highest in Europe. Furthermore, figure no. 2 illustrates the impact that regulation had on the monthly average consumption of SMS in France, corroborated with the corresponding evolution of the average retail revenue per SMS.

Figure no. 2 – Evolution of the monthly average SMS consumption, respectively average retail revenue per SMS



Smartphone penetration is at present 53% in France and only 57% of those smartphone users have downloaded IM applications. While ARCEP foresees that smartphone penetration will increase up to 77% of handsets in 2017, the rate of SMS consumption is expected to remain high in the coming years. ARCEP considers that the SMS services are a significant means of communication in some communities and makes special reference to low-income earners.

ARCEP also states that by deregulating the market, SMS volumes would, most likely, decrease, while there might be an impact on the development of alternative messaging services. However, in ARCEP’s view, such a market development would lower consumers’ welfare due to the following main reasons: IM services appeared late in the market, be it a consequence of path dependence or not, and a substantial part of the mobile users would not be able to access alternative messaging services.

Thus, ARCEP foresees competition risks if SMS termination rates were deregulated in view of a probable increase in SMS termination rates and an increase in dispute settlements concerning the likely asymmetries in SMS termination rates charged by new entrants, for example. Furthermore, this would trigger problems at the retail level, with profitability of some retail offers possibly becoming compromised and an increased exposure to risks of traffic asymmetries (on-net compared to off-net).

In the view of the development of IM services, ARCEP does not identify any barriers to their take-up. ARCEP considers that the SMP assessment and the regulation of the SMS termination rates does not hamper the commercial evolution of IM services, rather, it creates a level playing field in which competition is based on merits of each platform.

ARCEP lists several possible reasons for the slower take-up of IM services in France:

- the number of data broadband subscriptions and the smartphone penetration are lower in France when compared to other European countries;
- IM applications penetration is relatively low in France, the usage of these services being even lower. ARCEP states that this could be explained by the people's perception that they do not derive additional benefits from using such application-based IM services;
- evidence shows that a significant number of customers are not active users of IM services even though they have downloaded the relevant applications; and
- IM services lack interoperability.

To conclude, given that IM take-up as well as mobile internet take-up are limited in France, accounting for the fact that users of IM services must have a compatible equipment, and for all the aforementioned reasons, including the retail market delineation, ARCEP believes that the potential constraints stemming from OTT services are not strong enough to limit the possibility of an SMP operator to act independent of its clients, customers and, ultimately, consumers. Also, ARCEP considers that the proposed regulation does not hamper the development of IM services.

BEREC's Assessment

As previously mentioned, although BEREC agrees with the Commission to the extent that potential substitutes such as IM services from OTT providers should be considered in the market analysis for the provision of SMS services at retail level, BEREC does not share the Commission's serious doubt on the possibility of defining a broader market for SMS termination in France.

However, in BEREC's opinion the Commission is right in raising the issue that, even if IM services were rightly excluded from the relevant market definition, ARCEP should have thoroughly assessed constraints coming from these services at the stage of the SMP analysis.

Considering the entirety of the information provided about the OTT services in France and the fact that the use of OTT services is not necessarily bound by a mobile network operator (it can also be used when the smartphone is connected through Wi-Fi in any other data network), BEREC considers that ARCEP seems to have considered the competitive pressures exerted by the IM services on the wholesale market for SMS termination. Furthermore, the Commission's comments, that even if IM services were rightly excluded from the market definition, ARCEP should have thoroughly assessed constraints coming from these services at the stage of the SMP analysis, were considered by ARCEP and reported in the answers to the BEREC's questions during the meeting on 9 December 2014.

At the wholesale level, similar to the situation in the markets for voice termination, each network operator does not face countervailing buyer power, as each network operator has a monopolistic position on the market for SMS termination on its own network, but no say on the SMS termination rates for SMS termination on another network. Typically, the wholesale

charge of an SMS should also be recovered from the retail market. Given that the “unlimited SMS” offers on low-end bundles are considered a normal practice in France, and due to the fact that past events led ARCEP to believe that deregulating the market would create the risk that some operators increased the SMS termination rate for SMS messages terminating on their network, the operators would have two choices:

1. Either to absorb the possible increase in termination rates, while still providing the “unlimited SMS” offers, thereby decreasing their profit margins where possible;
2. Or, limit the “unlimited SMS” offers, thereby increasing retail prices for consumers.

BEREC is of the opinion that the comparison regarding the SMS termination charge in France (1 eurocent/SMS), which is considerably lower than the average termination charge in Europe (2.5 eurocent/SMS), is not appropriate. When determining whether an SMS termination rate is high, national circumstances of the market should be considered, in particular with respect to the associated costs of the provision of the service. ARCEP explains that consumers in France are accustomed to “unlimited SMS” offers. If, by deregulating the market, the average SMS termination rate in France increased, by say 100%, the SMS termination rate would still be lower than the EU average. However, it might determine operators to change retail prices to reflect higher wholesale costs and higher financial risks. Notwithstanding the above, BEREC does not know to what extent deregulation of the market would potentially increase wholesale charges for operators or the corresponding retail prices.

Finally, BEREC acknowledges that deregulation of the SMS termination market in France may potentially affect the consumer welfare, but more in-depth information is needed to draw a conclusion on whether consumer welfare would be negatively impacted and to what extent.

BEREC considers that ARCEP has examined competitive pressures exerted by the IM services on the wholesale market for SMS termination. However ARCEP should have made that analysis more explicit in the notified documents. Therefore BEREC finds the third serious doubt of the Commission partially justified.

5. CONCLUSIONS

On the basis of the analysis set out in section 4 above, BEREC considers that the Commission’s serious doubts regarding the draft decision of the French Regulatory Authority on the need to analyse competitive constraints on a forward looking basis, a potentially broader market for SMS termination in France and SMP assessment – as expressed in the EC’s serious doubts letter to ARCEP of 28 November 2014 – are partially justified.

BEREC is of the opinion that the Commission’s first serious doubt, as far as the need to analyse the competitive constraints on a forward looking perspective and, as well as the pressures from IM services in the vertically associated retail market, are only partially justified. ARCEP should have more clearly examined in its draft decision the current and future relation between SMS services and IM services, and their impact on the competition in SMS termination market, providing the supportive evidence in its notification. Due to the fact that ARCEP provided the aforementioned information to BEREC and in a later stage to the Commission, BEREC suggests that ARCEP should also incorporate the analysis into the final decision.

With respect to the second serious doubt, BEREC considers that the Commission's concerns are also related to the definition of the retail market, in the view of the interdependence between the retail and the wholesale market, and not solely to the definition of the wholesale market. However, as termination services are the last replicable element in an electronic communications network, the provision of services on the retail market is dependent on the provision of termination services at wholesale level. In this view, there is no doubt that, should a termination market be found as susceptible to *ex ante* regulation, the relevant market will be defined as comprising the termination services on each operator's network. Therefore, based on the evidence presented by ARCEP during the Phase II procedure (although not included in the original notification), BEREC does not share the Commission's serious doubt on the possibility of defining a broader market for SMS termination in France.

When it comes to the third serious doubt, BEREC considers that ARCEP has examined competitive pressures exerted by the IM services on the wholesale market for SMS termination.

Finally, BEREC acknowledges that deregulation of the market for SMS termination in France may potentially affect consumer welfare, but more in-depth information is needed to draw a conclusion on whether consumer welfare would be negatively impacted and to what extent. BEREC finds the third serious doubt of the Commission partially justified.

In light of the Commission's serious doubts and the argumentation above, BEREC would recommend that ARCEP should integrate the additional supportive evidence, that was presented to both the Commission and BEREC, into the final decision, specifically the supportive evidence regarding future developments of SMS and IM services, and the research concerning the substitution possibilities and potential competitive constraints concerning the analysed services, in the time frame of the market review.