

## **Summary report for stakeholders on the internal workshop on ERT/margin squeeze tests applied by NRAs on 11 October 2019 - Remedies WG**

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## Contents

Executive Summary .....	2
Introduction.....	2
Background .....	2
Observations from the workshop and next steps .....	3

## Executive Summary

This is the summary report of the internal workshop that was run by the Remedies Working Group. This internal workshop's purpose was to enable NRAs to discuss the insights regarding the "Economic Replicability Test" (ERT) as set out in Recommendation 2013/466/EU, the BEREC Guidance document from 2014 stemming from NRAs' experiences in applying ex-ante margin squeeze tests since then.

The workshop necessarily focused on such interesting topics as the methodological choices to be made by NRAs in conducting ex-ante margin squeezes in the telecommunications sector as well as difficulties in the practical implementation of margin squeezes.

Participants actively engaged on such topics as diverse as the inclusion of unregulated products in a bundle, to the time horizon for the assessment of the offer, and how to deal with temporary discounts/promotions.

Four NRAs presented on their approaches to margin squeeze tests for the purpose of enlightening the discussions.

## Introduction

The workshop was chaired by Dr. Annegret Groebel, BEREC Co-Chair of the Remedies Working Group, who firstly welcomed the 13 NRAs physically in attendance, and the 10 NRAs connected remotely, then ran through the planned agenda, and purpose of the meeting. Representatives of the BEREC Office and the EC were also in attendance.

## Background

The BEREC 2019 Work Programme committed the Remedies Working Group to undertake an internal workshop for NRAs in Q3 2019 on margin squeeze tests (MST), and to prepare a summary report for adoption at Plenary 4 2019.

The workshop's aim was to discuss the application of the "Economic Replicability Test" (ERT) as set out in Recommendation 2013/466/EU, the BEREC Guidance document and the experience of NRAs in applying ex-ante margin squeeze tests, i.e. the economic rationale of margin squeeze tests, the methodological choices to be made as well as difficulties in practical implementation.

The ERT is an ex-ante margin squeeze test, i.e. a test applied by NRAs when imposing price control obligations. In 2014, BEREC developed Guidance on the regulatory accounting approach to the ERT (BoR (14) 190). A key point to note is that the ERT was primarily focused on standalone products – i.e. not bundled services. Given the increasing prevalence of broadband products to be bundled in some form with one or more services – e.g. content such as soccer matches, mobile phone services, then the purpose and approach from a regulator needs to reflect this wider context.

## Observations from the workshop and next steps

1. The telecommunications sector is typically characterised by the presence of vertically integrated network operators who are obliged to provide access to their wholesale network to their competitors.
2. The reason that a margin squeeze of some form is required is that alternative operators (competitors) often depend on wholesale services of operators with significant market power (SMP) as an essential input into their own retail services (e.g. broadband). By setting either wholesale or retail prices (or both), the SMP-operator which are in principle vertically integrated firms, is able to define the space (margin) between the wholesale and the retail price level. By setting the margin too small, the SMP operator could potentially squeeze other operators out of the market. An ex-ante margin squeeze test is a means to identify and prevent such a situation. Thus an ex-ante margin squeeze test defines a minimum distance between a retail price and a wholesale price (or between two wholesale prices at different stages of the value chain respectively).
3. As such the application of ex-ante margin squeeze tests have received considerable attention in electronic communication markets. In a convergent world competition among operators is increasingly occurring via multi-play offers, where various services (e.g. voice, data, but also sports / video content) are being provided in a retail bundle at a single price. This bundling of services requires NRAs to carry out ex-ante margin squeeze assessments, particularly where bundled offers include regulated and unregulated components.
4. The workshop outlined the previous work undertaken by BEREC in this area namely, the BEREC Guidance document on EC Recommendation 2013/466/EU. The BEREC Guidance of 2014 was based on the experiences of NRAs up to that point. Since then though NRAs have noticed an increase of bundling and convergence in services driven by for example, the increased roll-out of fibre based access service thereby permitting other services such as IPTV, VoIP, etc. compared to what legacy (copper) access could support.
5. Four NRAs shared their experiences of ERTs and outlined particular aspects of ERTs undertaken by those NRAs. Each NRA outlined the purpose of their ex-ante margin squeeze tests (including bundles with unregulated services), the wholesale products assessed (e.g. "flagship" ones, or all relevant wholesale inputs), cost calculation methods used, relevant time periods for assessments, how discounts/promotions are handled, etc. NRAs also outlined their assessment process.
6. Following each presentation, a discussion ensued. A number of common items occurred a number of times, e.g. how to handle unregulated services such as content, the definition of a flagship product and changes to what is considered "the flagship" over time, etc.
7. Finally, the possibility of potential further work was also discussed, and a general agreement was that the Reg. Accounting in Practice Report for 2020 would seek more information on the operation of ex-ante margin squeeze tests by NRAs.