



PÓST- OG FJARSKIPTASTOFNUN

PTA Draft Decision no. xx/2015

On the designation of an undertaking with significant market power and on the imposition of obligations on the wholesale market for trunk segments of leased lines

(Previously Market 14)

The Post and Telecom Administration in Iceland (PTA) has, with reference to Article 17 of the Electronic Communications Act no. 81/2003, as amended, analysed the wholesale market for trunk segments of leased lines. Specifically this is the market that was no. 14 in the older ESA Recommendation on the relevant market from 2004:

- Wholesale market for trunk segments of leased lines.

With a letter dated 23 December 2013 a draft analysis of the above markets was sent to electronic communications companies and to the Competition Authority and they were invited to make comments on the market analysis and on its conclusions. The consultation ended on 24 February 2015. The Competition Authority, FjarSKIPTI ehf (Vodafone) and Mila ehf (Mila) submitted comments on the preliminary draft.

The analysis of the said market has now been updated in accordance with those observations that were taken into account. The updated analysis can be found in Appendix A to this Decision, and the comments that were received have been answered in Appendix B.

1. Designation of an undertaking with significant market power

Siminn hf. (Siminn) and Mila ehf were designated as having significant market power on the relevant market in PTA Decision no. 20/2007.

The conclusion of the analysis in this instance is that circumstances on the market do not differ essentially from the circumstances that pertained in 2007. All wholesale of leased lines within the Siminn Group has been transferred to Mila which means that Siminn therefore no longer operates on this market.

With a view to the market definition and analysis of competition on the wholesale market for trunk segments of leased lines and pursuant to Paragraph 2 Article 17, see Article 18 of the Electronic Communications Act, the PTA plans to designate Mila as still having significant market power on the relevant market, while the Siminn designation will be withdrawn.

2. Imposition of obligations on Mila ehf on the market for trunk segments of leased lines

With the PTA Decision no. 20/2007, obligations were imposed on Mila and Siminn on the relevant market for access, non-discrimination, transparency, accounting separation and price control, including cost accounting.

In accordance with Article 27 on the Electronic Communications Act, the PTA intends to maintain the following obligations on Mila ehf subsequent to the planned designation of the undertaking as having significant market power on the relevant wholesale market.

Those obligations that were imposed on Mila ehf in 2007 and that the PTA intends to maintain are mostly unchanged. There are however various amendments to implementation, such as with respect to the methodology for cost analysis and to the publication of bookkeeping information. In addition to this the obligation for non-discrimination is more precisely elaborated, e.g. regarding provisions for a period of notice for notifications, the making of service level agreements, service level guarantees and the publication of key performance indicators. In the opinion of the PTA these obligations are both in accordance with the objectives presented in the EU Framework and Access Directives and with the provisions of legislation on electronic communications and are appropriate for the period of time that is expected to pass until the market will be analysed again. The PTA considers that the obligations are conducive to increasing competition on the relevant market. With respect to further discussion on the obligations the PTA refers to the revised analysis on the said market, see Appendix A.

The intention is that the following obligations replaces the obligations imposed on Mila with the PTA Decision no. 20/2007 from 14 September 2007. Further details are provided on the imposed obligations in Appendix A to this draft Decision.

2.1 Obligation to provide access

With the authority in Articles 28 and 33 of the Electronic Communications Act the PTA plans to impose the obligation on Mila to accommodate normal and fair requests for access to trunk segments of leased lines and related service at wholesale level. Mila shall among other things accede to normal and fair requests for access to resale, joint utilisation or co-location, open access and technical interfaces, communications protocols and other technology that assures interactive service and interconnection of networks, access to support systems and appropriate information and in addition to this Mila shall announce all technical migration with a specific period of notice.

More precisely, Mila shall provide a list of planned excavation and duct activities (Civil Works) with six months' notice. Mila shall notify parties to the market about all changes to system design that are likely to alter competitiveness of companies on the market, with at least five years notice, for example on decommissioning of systems or services.

Access that Mila has already provided for another party, whether through supply of leased lines or with access to facilities, may not be withdrawn without the agreement of the PTA. Mila ehf shall ensure that the service that is on offer will remain on offer for a reasonable period of time and it is only authorised to withdraw service after consultation with the relevant users and with the endorsement of the PTA. If a service is discontinued then the planned changes shall be notified to the electronic communications companies involved as soon as possible and no later than six months prior to the planned changes.

Agreements on access to and interconnection with the Mila leased line network shall be completed within a reasonable time scale and without undue delay. Denial of access shall be

justified in an adequate manner.

2.2 Obligation for non-discrimination

With the authority of Article 30 of the Electronic Communications Act the PTA intends to impose an obligation on Mila for non-discrimination on the wholesale market for trunk segments of leased lines, both with respect to price and other conditions. Mila shall provide all purchasers of leased lines, including its own units, with analogous terms of service, price, and quality of supply of data handling speeds, transport and communications protocols. Mila shall provide the PTA with a tariff for all speeds and all protocols and shall confirm that there is no difference in treatment of internal departments and of external parties in this respect.

Information on access to leased lines and related services shall be accessible to other electronic communications companies on an equal basis as to related parties, and the PTA considers it particularly important that Mila does not have the opportunity to discriminate in an abnormal manner between related and unrelated parties with respect to innovations on the market. Unrelated parties shall be informed about distribution, enlargement or other developments of Mila leased line services with the same notice as parties related to Mila and this notice shall not be shorter than six months. Mila shall also give related and unrelated parties the opportunity to influence development of new construction and planned interfaces.

In order to ensure that Mila fulfils the obligation in question the PTA can perform a technical and/or economic investigation as to whether unrelated parties can replicate the product offer of related parties in a sustainable manner. Should the PTA conclusion be such that unrelated parties cannot replicate the product offer of related parties for technical or economic reasons, the PTA can order Mila to change its product offer and/or offer new wholesale products such that unrelated parties can replicate the product offer of related parties with under normal commercial constraints.

The PTA plans to make the reservation that Mila make service level agreements (SLA's) with all purchasers of trunk segments of leased lines where among other things the quality of service shall be prescribed along with issues relating to non-discrimination, as itemised in the obligations that the PTA plans to impose on Mila on the relevant market. In addition to the obligation to make service level agreements the PTA intends to impose the obligation on Mila to issue a specific declaration on service level guarantees (SLG's). In order to ensure that Mila respects the obligation for non-discrimination and the making of service level guarantees, the PTA intends to impose the obligation on Mila that it should collect and publish regularly certain key performance indicators (KPI's). Service agreements, declaration on service level guarantee and key performance indicators shall be published within six months from the publication of the final Decision.

Mila shall arrange its operations in such a manner that the treatment of information is in accordance with Article 26 of the Electronic Communications Act. It is unauthorised to provide other parties with information on transactions with other companies with respect to potential purchase, including other departments in the Siminn Group, subsidiaries or partners.

2.3 Obligation for transparency

With the authority of Article 29 the PTA intends to impose the obligation on Mila for the publication of an itemised reference offer for trunk segments of leased lines and related facilities and service. Publication on the Mila website is deemed adequate. The reference offer should be broken down in accordance with the needs of the market and should contain a description of

Mila terms and conditions along with the relevant tariff. Mila shall publish a reference offer in accordance with the description here above and shall update it as required, such as for changes in needs of parties to the market or as a result of changes in technology. Should the Mila reference offer not be considered adequate for the market, the PTA could prescribe amendments to the offer pursuant to Paragraph 2 of the Electronic Communications Act. All changes to the reference offer shall be submitted to the PTA for endorsement with reasonable notice and they will not come into force without the endorsement of the PTA. Mila shall send all agreements made on wholesale trunk segments of leased lines to the PTA.

2.4 Obligation for accounting separation

With the authority in Article 31 of the Electronic Communications Act the PTA maintains obligations on Mila for accounting separation. Such separation shall constitute as a minimum that the operation of leased lines in wholesale is separated in the accounts from other operations. The Mila wholesale prices and internal prices within the company shall be transparent, among other things to prevent unjustified subsidies. In its accounts, Mila shall separate revenue, costs, assets and liabilities for access to trunk segments of its leased lines. Mila is required to submit separate profit and loss accounts annually to the PTA along with a balance sheet for the operations of leased lines and a statement of the division of indirect costs that cannot be allocated with comparison with other cost items. The above specified statement should have reached the Administration no later than five months after the end of the financial year. Mila shall at the same time deliver a report from an independent auditor to the PTA to show that there is correspondence between the Mila description to the PTA on how costs had been divided and the implementation of accounting separation by Mila.

2.5 Obligation for price control

With the authority of Article 32 of the Electronic Communications Act the PTA intends to impose the obligation on Mila for a cost oriented wholesale tariff for trunk segments of the company's leased lines. When deciding prices for trunk segments of leased lines, the cost analysis methodology shall be used which is based on historical costs allocated to the relevant service (HCA FAC).

When implementing its cost analysis Mila shall base its methodology on Chapter IV of Regulation no. 564/2011 on bookkeeping and cost analysis in the operations of the electronic communications companies, such as on evaluation of operating capital, life-cycle and ROI requirement. Furthermore, account shall be taken of the PTA position on criteria and calculations in the PTA Decision no. 7/2010 with respect to cost analysis for trunk segments of leased lines.

If the Mila cost analysis for trunk segments of leased lines returns a conclusion that the PTA considers unacceptable when one considers the development of price levels and tariffs on comparable competition markets, the PTA may request a review of that conclusion. The Administration will in such cases request that Mila reviews the criteria applied when evaluating Mila's assets used in providing the relevant service for the purpose of returning a conclusion which is in accordance with the above considerations and with the objectives of the EU Commission to support competition and to improve the investment environment on the electronic communications market.

The Mila cost analysis for wholesale tariff for trunk segments of leased lines shall be based on the following main criteria:

- Allocation of costs is based on accounting separation for a trunk line network, on Mila asset bookkeeping and on costs from Mila's bookkeeping system where operational costs are entered under bookkeeping accounts.
- The cost base is Mila historical costs (HCA).
- Operational costs are based on the preceding financial year in each instance. The methodology is based on allocating all costs to the service in question (FAC).
- When evaluating investments for leased lines, the reference shall be indexed historical costs. Gross replacement cost of operational assets shall also be taken into account, in the light of next generation networks (NGN).
- A depreciation methodology shall be used that reflects the value in use of an asset.
- Equivalent annual cost shall be used to calculate annual investment costs.
- The cost of the trunk line network shall be captured, including share of joint costs, management and IT and senior management in accordance with accounting separation.
- Real return on investment shall be used as a reference, based on WACC¹ real from capital bound in assets used in connection with providing service where the risk premium reflects the risk related to operations on the relevant market.
- The number of lines shall be calculated taking into account line equivalents. In assessment of line equivalent exponents one shall normally take into account costs in proportional context to the capacity and length of leased lines. In the case of new service it is authorised to take into account an estimate of the number of connections.
- Average base unit cost for the whole country and/or for specific categories of paths, is calculated from allocated operational and investment costs divided by number of lines or line equivalents.

Mila shall ensure at any given time that the tariffs list all wholesale service on the market for trunk segments of leased lines on offer by Mila to its own units and related companies. Furthermore Mila is obliged to review the product offer in its tariff in step with market requirements at any given time and if reasonable requests are received in accordance with the access obligation. All additions and amendments to the tariff shall be endorsed in advance by the PTA and do not come into force until such an endorsement has been granted, subsequent to national consultation and consultation with ESA and with other electronic communications regulatory bodies in the EEA.

Mila is authorised to offer tariffs by categories of paths if they are based on cost reference and if there is non-discrimination between parties.

The Mila tariffs for leased lines shall be easy to understand and shall take into account the following main principles:

- They shall be based on costs and on objective criteria such as distance and capacity.
- They shall take into account all service items included in the relevant service.

¹ In accordance with Article 16 of Regulation no. 564/2011 the PTA decides on an annual basis the weighted average cost of capital (WACC) which electronic communications companies should use as a reference in their calculations.

- They shall in general be divided into: Start-up charge (installation) and subscription charge (fixed lease charge for a specific period of time). Where another division is used (such as price per kilometre) it shall be based on objective criteria.

The Mila tariff for leased lines is now generally divided into start-up charge, subscription charge per month and kilometre charge per month. Exceptions to this rule are that the lease of dark fibre is based solely on a start-up charge and the distance charge (divided into urban and rural) and the tariff for Metropolitan Data Highway is based on a start-up charge and then a subscription charge per month. The PTA considers that Mila shall in the coming years aim towards amendments in its tariffs such that there will only be a price for a subscription charge per month independent of distance where possible and based on capacity and on the service items included in the service in question.

Finally, the PTA intends to prescribe that the Mila tariffs for trunk segments of leased lines be reviewed not later than before the end of 2016 and then annually, in accordance with updates of cost analysis in accordance with the development in number of units sold and costs. New wholesale tariffs for trunk segments of leased lines will not come into force until after endorsement by the PTA subsequent to national consultation and consultation with ESA in each instance.

2.6 Cost accounting

Pursuant to Article 32 of the Act on Electronic Communications, the PTA plans to impose the obligation for cost accounting on Mila for specific types of interconnection or for access, in accordance with a cost-oriented tariff. According to Chapter IV of Regulation no. 564/2011, on bookkeeping and cost analysis in the operations of electronic communications undertakings, an electronic communications undertaking with SMP on whom special obligations have been imposed pursuant to the Act on Electronic Communications shall inform the PTA on the structure of separation in bookkeeping, with respect to income and expenses, among other things for the user network and the backbone network. The PTA obligation for cost accounting covers those parts of the Mila electronic communications operations necessary for giving access to trunk segments of leased lines. Mila shall submit to the PTA a description of the cost accounting for trunk segments of leased lines which shall show among other things cost categories, cost items and their relationship with the cost driver.

Mila shall, no later than six months after the publication of the Decision on the relevant market, submit to the PTA a description of cost accounting for trunk segments of leased lines and related facilities and shall publish cost categories and rules used to allocate costs. Mila shall at the same time submit a report to the PTA from an independent auditor showing that there is correspondence between the Mila description to the PTA of how costs are split and the implementation in the Mila cost bookkeeping system.

3. The coming into force of the Decision and channels for appeal

This Decision comes into force from the day that it is published and will be in force until a Decision is made to the contrary by the Post and Telecom Administration.

This Decision can be appealed to the Appellate Committee for Electronic Communications and Postal Affairs, see Article 13 of Act no. 69/2003 on the Post and Telecom Administration. The appeal shall have reached the Appellate Committee four

weeks from the time that the party in question became aware of the Decision of the Post and Telecom Administration.

Reykjavík, 1 July 2015

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Attached:

Appendix A - Analysis of Market or trunk segments of leased lines

Appendix B - Comments by stakeholders and the conclusions from the national consultation