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**Swedish comments on the draft NGA recommendation of
090611**

Sweden welcomes the opportunity to comment on the new draft NGA recommendation and supports the objectives of the recommendation. It is important to have a recommendation which provides high principles and greater regulatory certainty for market players.

Having been in forefront of infrastructure sharing when licensing UMTS-networks, Sweden also welcomes the Commissions positive attitude to co-investment projects, which may lower investment risk and accelerate network roll-out.

There has been several improvements since the draft Recommendation of autumn 2008, e.g. this new draft has less focus on duct access and is less prescriptive concerning pricing methodologies. However, there are still some issues we would like to comment.

Imposing remedies

The purpose of a recommendation is to give guidelines regarding how the national legislation, implementing the relevant directives, should be applied. Hence, a recommendation must be based on the very reasoning in the directive. According to article 2 of the draft Recommendation, the purpose is to promote the consistent implementation of remedies with regard to NGA:s pursuant to Directive 2002/19/EC.

In article 8.2, directive 2002/19/EC states that

Where an operator is designated as having significant market power on a specific market as a result of a market analysis carried out in accordance with Article 16 of Directive 2002/21/EC (Framework Directive), national regulatory authorities shall impose the obligations set out in Articles 9 to 13 of this Directive as appropriate.

and in art 8.4

Obligations imposed in accordance with this Article shall be based on the nature of the problem identified, proportionate and justified in the light of the objectives laid down in Article 8 of Directive 2002/21/EC (Framework Directive). Such obligations shall only be imposed following consultation in accordance with Articles 6 and 7 of that Directive.

This procedure for imposing obligations has been incorporated in Swedish law, and requires the NRA to motivate in detail why a certain remedy is appropriate and proportional in every case. The appropriateness of remedies should result from a thorough analysis taking into account the specific circumstances in the country in question.

However, many articles in the draft recommendation, e.g. art 11, 12 and 15, state that the NRA should impose a specific obligation regardless of the nature of the problem and the specific national circumstances. In practise, this means that the NRA should ignore the procedure prescribed in art 8.4 of the Directive this recommendation is supposed to help implement. If a NRA was to apply this recommendation when imposing obligations, such decisions would not be based on sufficient legal grounds, and would not hold up in court in case of an appeal.

The Commission should therefore address these concerns and make the necessary adjustments.

Regulatory exemptions

Under certain circumstances, e.g. deployment of multiple fibre or joint investments, the draft Recommendation prescribes exemptions from certain remedies, e.g. cost-oriented pricing or non-discrimination.

If some areas or networks are exempt from an obligation of price control, this implies that the competition problems on which the decision to impose price control was based does not exist in this area. According to market analysis practice in competition law, such different circumstances indicate that the network in question is a separate market. Any lighter regulatory regime should hence be based on a separate market analysis for the local market/network in question, and can not be part of national market regulation. Hence, the proposed exemptions contradict the principles of competition law.

The principle of equivalence

Within competition law and telecom regulation, the “principle of non-discrimination” is legally well defined. Also, according to art 10 of the Access Directive, NRA:s can impose an obligation of non-discrimination. The directives give however no legal ground for NRA:s to impose an obligation to provide access in accordance with the principle of equivalence. Hence, with the present wording, the Recommendation can not be applied on this point. The Commission should replace all references to “the principle of equivalence” with references to “the principle of non-discrimination”.

The recommendation

Access to wholesale physical network infrastructure (market 4)

Access to civil engineering infrastructure of the SMP operator

As stated above, it is impossible to recommend that a certain remedy, be it access, cost-orientation or reference offer, is always proportionate and justified regardless of the competition problem.

Also, the NRA is not a provider, nor a middle man, in the provision of ducts. Establishing operating procedures and parameters is part of an obligation for the SMP to provide access to ducts.

It is also recommended that NRAs should oblige the SMP operator, when building civil engineering infrastructure, to install sufficient capacity for other operators to make use of these facilities. In Sweden, the NRA has no mandate to prescribe for the SMP what infrastructure should be built and how. A NRA should be careful not to encourage or oblige investments which may be economically unfeasible and could harm the SMP without doing benefit to anyone else, hence being unproportional.

Access to the terminating segment in the case of FTTH

It is recommended that NRAs should mandate access to wiring inside buildings. According to Swedish law, the wiring inside buildings is part of the building, unless otherwise explicitly stated. Hence, access can only be mandated to the network termination point.

It is also recommended that the NRA should determine where the distribution point of the terminating segment of the access network should be for the purpose of mandating access. However, an obligation to provide access is usually expressed as an obligation for the SMP-operator to meet every reasonable request for access. This means that access should be provided where the purchasing operator so requires, and where it is technically feasible. As the future developments of NGA are very uncertain regarding choice of technology over time in different member states, Sweden wants to stress the importance of not limiting the access possibilities for purchasing operators by determining distribution points in the network hierarchy in advance.

There is also a recommendation that NRAs should encourage or oblige the SMP operator to deploy multiple fibre lines in the terminating segment. However, the aim of regulation is not only to create competition, but also to create a positive climate for investment. It is up to the investing operator to judge what technology and network structure to deploy based on the individual business case. Whether to deploy multiple fibre lines to reach the users premises or just a few lines with multiplexed traffic (CWDM or DWDM), is not a decision for the regulator, nor something the regulator can make recommendations about. As stated in art. 8.1 of the Framework Directive, the regulation should be technology neutral.

Unbundled access to the fibre loop in the case of FTTH

The Commission recommends that the existing LLU reference offer should be complemented to include unbundled access to the fibre loop. For the Commission to give detailed directions on how the SMP operator should make the fibre offer public is too prescriptive.

It is also recommended that NRAs should assess pricing schemes proposed by the SMP operator according to certain criteria from the Commission. However, assessing price schemes or discriminatory behaviour is part of the NRA:s supervisory activities. How each NRA should perform its supervision is hardly a matter to be decided in detail on European level. This is overly prescriptive.

As stated above, the proposed exemptions from an obligation of cost-orientation contradict the principles of competition law. Also, the basis for the exemption is a cooperation between operators under circumstances that might suggest joint dominance. The condition for refraining from cost-orientation may be achieved easily by the SMP operator, as the SMP will only need to grant access to one other operator.

There is also a contradictory reasoning that even if there is no price control obligation, there should still be price control to some extent. If there is no price regulation of access, competition problems based on overpricing or margin squeeze should be treated according to competition law by the national competition authority. The Swedish NRA does not have a mandate to apply competition law on unregulated sectors, i.e. apply a margin squeeze test.

The Commission also states that NRAs should normally presume the absence of SMP in areas where joint deployment of FTTH networks based on multiple fibre lines takes place. In case of anti-competitive co-ordinated behaviour, NRAs should impose cost-oriented access. However, according to Competition Law, if there is no SMP, there are different circumstances than on the rest of the market, indicating this is a separate market. Any presumption of no operator having SMP should be made after a market analysis of this local market. In case of anti-competitive co-ordinated behaviour, it is likely an abuse of dominant position, indicating that there is an SMP. The only way the NRA can impose price control is after finding an SMP on the market.

Access obligations in the case of FTTN

The Commission recommends that the existing LLU reference offer should be complemented to include all items necessary for sub-loop unbundling. For the Commission to give detailed directions on how the SMP operator should make the sub-loop offer public is too prescriptive.

Wholesale broadband access (market 5)

For market 5, it is recommended that NRAs should consider wholesale broadband access over VDSL as a chain substitute to existing wholesale broadband access over copper-only loops. However, both xDSL variants, VDSL as well as ADSL, use copper-only loops. Whether or not VDSL is a substitute to existing bitstream access is part of the definition of the relevant market, hence this sentence belongs in the recommendation on relevant markets and should be removed from this recommendation.

It is also recommended that NRAs should oblige the SMP operator to make new wholesale broadband access products available at least six months before the SMP operator or its retail subsidiary markets its own corresponding NGA retail services. The NRA can impose a proportional obligation to provide access on non-discriminatory conditions, and to meet every reasonable request for access. However, to oblige the SMP a six months waiting period between introducing its new wholesale service until it can use it in its own business is obviously not proportional. It must be up to the NRAs to decide how long a proportional waiting period is.

The Commission also states that NRAs should cooperate with each other in order to define appropriate technical specifications for wholesale broadband access products provided over NGAs. However, the European cooperation in technical matters is run through ETSI, consisting of industry, operators and regulators, which defines all European standards. There is no need for NRAs to specifically cooperate on this issue.

As previously stated, the proposed exemptions from an obligation of cost-orientation contradict the principles of competition law, and the basis for exemption is a cooperation between operators under circumstances that might suggest joint dominance.

The Commission also recommends that where NRAs consider that there is effective access to the unbundled fibre loop of the SMP operator's network and that such access is likely to result in effective competition on the downstream market, NRAs normally should not impose an obligation of wholesale bitstream access. However, whether or not bitstream obligations should be imposed is decided as a result of a market analysis of market 5, not as a result of an analysis of market 4. If there is effective competition on market 5, there is no SMP and no obligations. Regarding the absence of SMP, any presumption of no operator having SMP should be made after a market analysis of this local market.

Migration

The Commission recommends that NRAs should put in place a transparent framework for the migration from copper to fibre-based networks. As with ducts, the NRA is not a provider, nor a middle man, in the provision of fibre. Establishing operating procedures and parameters is part of an obligation for the SMP to provide access. The NRA will supervise the proper function.

Annex I

Pricing principles and risk

General comments

The concept of a “risk premium” is not used consistently throughout the recommendation. A number of seemingly arbitrary presumptions with regard to the level of the risk premium are made without analysing the risk by assessing the uncertainties faced by the investor.

According to the Recommendation, access to civil engineering should not include a risk premium. This seems to imply that such investments do not have any risks at all, which may not be the case. Access to the terminating segment in the case of FttH includes a risk premium where appropriate to reflect additional and quantifiable risk. This seems to imply that a risk premium should be added in each specific case where appropriate, which would create regulatory uncertainty, and be practically not doable. Access to unbundled fibre loop should include a risk premium, while for sub-loop unbundling in the case of FttN no risk premium is mentioned. A risk premium is applicable for FttH, but not for FttN. For WBA based on VDSL risk should not be presumed to be of similar magnitude as the FttH based wholesale access products.

The Commission must explain the basis on which these proposals are based. These presumptions could pre-empt a proper analysis of the roll-out. This inconsistent use of the concept of a “risk-premium” risks steering the choice of technologies in one direction thus potentially distorting investment decisions.

Common principles for the pricing of NGA access

The Commission proposes that NRAs should consider whether duplication of the relevant NGA access infrastructure is economically feasible and efficient. It is difficult to understand what the Commission actually means with this proposal. Whether duplication of network infrastructure is feasible is in each separate case a matter of commercial considerations by the market players. It is not clear if the NRA should make this consideration on a general, national level, for the replication of ducts in general or fibre in general or networks in general, or on a case by case basis for local network areas or municipalities. A general decision that duplication of ducts or fibre is generally feasible on a national level is impossible to make, because of the local differences. For the NRA to evaluate whether duplication is feasible on a case by case basis for separate network areas is impossible, and would also mean that there is no regulatory certainty at all.

The Commission also recommends that a consistent regulatory approach may imply that NRAs use different cost bases for the calculation of cost-oriented prices for replicable and non-replicable assets, or at least adjust the parameters underpinning their cost methodologies in the latter case. The use of different cost bases will result in many practical problems regarding cost-

models, and would rather be inconsistent. To use different cost bases case by case would be impossible and create total regulatory uncertainty.

The Commission also wants NRAs to assess whether a risk premium should be included in the cost of capital in specific cases. This implies that the NRA should analyse individual network investment projects in order to add an extra risk premium in a specific area if necessary, which would lead to total regulatory uncertainty and an excessive administrative burden for the NRA.

It is further recommended that the price of access to physical network infrastructure should not be a geographical average in the presence of substantial cost differences between various areas. This recommendation of not averaging access pricing needs to be developed more regarding its purpose and what consequences it will have on consumer prices in different regions.

Also, it is recommended that NRAs should perform margin-squeeze tests when monitoring prices. Today's regulatory principles uses wholesale regulation and no regulation of end-user prices. The NRA can only make certain that the SMP have a correct pricing according to the cost based price regulation of wholesale elements. If the end-user price is too low, creating a margin squeeze, it is a matter for the national competition authorities to deal with according to Competition Law.

Regarding the estimation of the costs for access, these principles have been discussed and described in detail and at length in directives and recommendations in the 1990:s, ending in a recommendation to use LRIC for cost based price regulation.

Pricing of access to civil engineering infrastructure

The Commission recommends that access to existing civil engineering infrastructure should be mandated at cost-oriented prices, and access prices should reflect the costs effectively borne by the SMP operator. The meaning of the expression "the costs effectively borne" is very unclear. It is most likely not the incremental cost of an effective operator, it could be the historical cost, it could be margin cost, or it could be the alternative cost for the SMP of not using the fibre itself. As there are well defined expressions in the literature like historical cost, incremental cost/LRIC and margin cost, the Commission should avoid introducing expressions that are not properly defined and will create a random application among member states.

Also, NRAs are advised in particular to take into account actual lifetimes of the relevant infrastructure and possible deployment economies of the SMP operator. Access prices should capture the proper value of the infrastructure concerned, including its depreciation. As stated in ERG:s response to the previous draft in September 2008, this can be interpreted in a way where ducts would have to be considered one by one, which is unrealistic. Also, the regulatory accounting of the SMP:s is generally nation wide.

Pricing of access to the terminating segment in the case of FTTH

As stated above, the expression “the costs effectively borne” is not properly defined.

Pricing of access to the sub-loop in the case of FTTN

Here, the Commission recommends that regulated access prices should not be higher than the cost incurred by an efficient operator, and that NRAs may consider to evaluate these costs using bottom-up modelling or benchmarks, where available. As with “the costs effectively borne” this is very unclear. Although the wording “an efficient operator” and “bottom-up modelling” reminds of LRIC-calculation, it is too vague. In its recommendation of 25 May 2000, on LLUB including sub-loop unbundling, the Commission recommends a forward looking approach based on current costs, i.e. LRIC. LRIC has since become a standard for cost based pricing, and its use for cost calculation is explicitly recommended by the Swedish legislator. If the Commission means that LRIC should be used, this must be clarified, if an other method than LRIC should be used, it must be explicitly stated.

Criteria for setting the risk premium

The Commission proposes that NRAs, when calculating the WACC, should take into account all dimensions of capital employed, including appropriate labour costs, building costs, anticipated efficiency gains etc. However, the formula for calculating Weighted Average Cost of Capital is well defined in the literature. If the Commission wants NRAs to use an other formula, it will not be WACC.

The NRAs have for several years practised cost calculation, including calculating the rate of return, in a LRIC-environment as well as historic cost environment. These existing practices are as valid when calculating in an NGA environment. The WACC combined with a risk premium should reflect the estimated financial risk taken by the investor at the time of considering whether to make an investment or not. This estimation includes considerations regarding end-user uptake, wholesale contract lengths and how many fibre loops that will be used, and covers the economical lifetime of the investment. The consideration also includes the possibility of a failed investment, or the possibility that the investment will give better revenue than expected. The regulated access price will include a reasonable rate of return based on WACC including a risk premium, which in turn is part of the rate of return on equity reflecting the risk associated with the investment. There is no need to add an extra risk premium to the rate of return on equity.

General comment on discounts for long term contracts and volumes

It is in the interest of the investor to have wholesale customers that sign long term contracts with high volumes. It not only reduces risk, it also reduces cost. Hence, it is in the interest of the investor as well as the wholesale customers to have discounts that reflects not only the risk reduction, but also the cost reduction. A regulation that limits possible discounts to the amount of the risk premium would most likely not be

appreciated by the wholesale customers, who will not be able to benefit from the economies of scale.

Criteria to assess long term access pricing in case of FTTH

The Commission proposes that wholesale customers signing long-term contracts for fibre access should have the possibility to engage in secondary trading. However, the purpose of network infrastructure access regulation is to give operators an opportunity to attach their own active equipment to the SMP:s physical media in order to provide broadband services to end users, and wholesale broadband services to other operators. The SMP has no obligation to provide access for the purpose of reselling physical transmission media. Not only would such a possibility reduce the SMP-operators control of its network, the secondary trader would be able to block the usage of a specific subscriber line if the third hand wholesale customer do not pay a higher price than cost based. Hence, such secondary trading would reduce the regulatory value of a price control obligation.

Price discounts based on contract times has for a long time been a common principle on the Swedish market for leased lines. The annual cost of providing a service during a long time is normally lower than when providing it for a short period, which may be reflected in the price. There is no reason for the NRA to prevent big wholesale customers from getting a discount that reflects the cost reduction as well as the lower financial risk. There is no reason to interfere with these pricing schemes, as long as they are non-discriminatory, transparent and does not favour the incumbents subdivisions. If so, it is a matter for NRA supervision.

In order to prevent abuse of volume discounts, the Commission also sets the condition that the SMP-operator should have a sufficient margin between wholesale and retail prices to allow for market entry by an efficient competitor in the downstream market. This kind of regulation is an obligation called price control by retail-minus and can not be combined with a cost based wholesale price model. Today's regulatory principles uses wholesale regulation and no regulation of end-user prices. The NRA can only make certain that the SMP have a correct pricing according to the cost based price regulation of wholesale elements. If the end-user price is to low, creating a margin squeeze, it is a matter for the national competition authorities to deal with according to Competition Law.

Criteria to assess volume discounts in case of FTTH

The Commission proposes that access prices could vary in accordance with volume purchased, and that volume discounts should only reflect the reduction of risk for the investor. Such an obligation, to successively update local prices in relation to the amount of fibres used in a specific area, creates a very flexible pricing scheme which would be difficult to include in a reference offer. It also creates an unproportional work load on the SMP and raises questions regarding if all contracts should be reviewed and updated each time, or if the new price only should apply to new contracts. This proposal is very hard to carry through.

The Commission also sets the condition that volume discounts should only be accepted if there is a sufficient margin between wholesale and retail prices to allow for market entry by a reasonably efficient service provider in the downstream market. As stated above, the price should be based on cost. The notion of a price that “allows for market entry by a reasonably efficient service provider in the downstream market” is part of the theory about price regulation through the “retail minus”-method.

Annex II

Application of the principle of equivalence for access to the civil engineering infrastructure of the SMP operator for the purpose of rolling out NGA networks

As stated above, within competition law and telecom regulation, the “principle of non-discrimination” is legally well defined. According to art 10, NRA:s can impose an obligation of non-discrimination. The directives give however no legal support for NRA:s to impose an obligation to provide access in accordance with the principle of equivalence. What is described below is how the SMP should act when providing access in accordance with the non-discrimination obligation. The principle has been described in earlier directives, recommendations and ERG CP:s.

Also, the supervision of discriminatory behaviour is part of the NRA:s supervisory activities. How each NRA should perform its supervision is hardly a matter to be decided in detail on European level. This is too prescriptive.

Annex III

Regulated access to the unbundled fibre loop in case of co-investment into FTTH

Conditions under which cost-orientation is not justified

As stated above, if some areas or networks are exempt from an obligation of price control, this implies that the competition problems on which the decision to impose price control was based does not exist in this area. According to market analysis practice in competition law, such different circumstances indicate that the network in question is a separate market. Any lighter regulatory regime should hence be based on a separate market analysis for the local market/network in question, and can not be part of national market regulation. It is questionable if this proposal is in accordance with the principles of competition law.

Conditions under which the absence of SMP should normally be presumed

As above, if there is no SMP, there are different circumstances than on the rest of the market, indicating this is a separate market. According to competition law, any presumption of no operator having SMP should be made after a market analysis of this local market.