Commission for
Communications Regulation

Consultation and Draft Directions

Review of the appropriate price controls in the markets of Retail Fixed Narrowband Access, Wholesale Physical Network Infrastructure Access and Wholesale Broadband Access:

Further specification of certain price control obligations in the markets of Retail Fixed Narrowband Access and Wholesale Physical Network Infrastructure Access

Document No:	**11 / 72**
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All responses to this consultation should be clearly marked:- "Reference: Submission re ComReg 11/72" as indicated above, and sent by post, facsimile or e-mail to arrive on or before 5pm, 21 November 2011, to:

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Please note ComReg will publish all respondents' submissions with the Response to this Consultation, subject to the provisions of ComReg's guidelines on the treatment of confidential information – ComReg Document No. 05/24

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1 Introduction

1.1 The principal aim of this consultation is to consider whether ComReg should further specify the regulatory controls in place which govern how Eircom sells bundles. The controls are intended to ensure that Eircom bundles that include retail line rental ("retail fixed narrowband access") are not priced in such a way as to force Other Authorised Operators ("OAOs") which use Eircom's network to sell their retail bundles at a loss. This could happen because Eircom is dominant in the provision of line rental and is, in ComReg's view, able to leverage this position into related markets such as those for calls and broadband. In addition, Eircom is also dominant in upstream wholesale markets. This means that OAOs must source important components for their services from Eircom itself. If the gap between what Eircom sells wholesale services for and its own retail bundle prices is too narrow, and in particular does not at least cover Eircom's retail and other unavoidable costs, then these OAOs will be unable to compete at the retail level. The test that ComReg currently applies to do this is called a "net revenue test". The purpose of this net revenue test will stay the same but, with the prospect of more localised competition evolving over time, ComReg believes there may be merit in revising the parameters of the net revenue test such that regulation may be sufficiently responsive to any such developments if they occur. Much of this paper is concerned with how these retail costs should be measured and applied. The paper also discusses matters pertaining to an imminent new broadband only wholesale product (referred to in this paper as "Naked WBA (Bitstream) DSL" or "Naked WBA DSL") which is likely to be launched in 2012. It also discusses what controls may be necessary where unregulated services, in respect of which Eircom is not dominant, are bundled with services in respect of which Eircom is dominant or over which it can exert leverage. Finally, this consultation also proposes a margin/price squeeze test in the Wholesale Physical Network Infrastructure Access ('WPNIA') market – this was not in Consultation Document No. 10/01.

1.2 This consultation follows on from Consultation Document No. 10/01[1]. This further consultation is required given the passage of time and developments which have occurred in the market since then. In this further consultation, ComReg has considered the views of its expert consultants, Oxera[2].

1.3 This consultation does not address the regulation of services provided over Next Generation Access ("NGA") networks. This will be the subject of a separate consultation which will issue before a final decision on this paper will be taken. ComReg will ensure that responses to its planned NGA consultation are reviewed by it before issuing a final decision on this paper. This will help ensure a coherent approach is taken.

1.4 The remainder of this document is structured as follows:

- Chapter 2 provides an Executive Summary.
- Chapter 3 provides a background as to the evolving market for the provision of broadband in different areas of Ireland that needs to be considered in the revised

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[1] 'Consultation and draft direction: further specification of the obligation not to unreasonably bundle pursuant to D07/61' dated 6 January 2010

[2] For information purposes only, their report is published as ComReg Document No. 11/72a. Oxera's views expressed are not necessarily the views of ComReg.

net revenue test proposed in Chapter 4 and the possible margin squeeze test in WBA of Chapter 9.

- Chapter 4 details the proposed revisions to the net revenue test in the markets of Retail Fixed Narrowband Access.
- Chapter 5 details the proposed revisions to the wholesale input cost in the net revenue test in the markets of Retail Fixed Narrowband Access.
- Chapter 6 summarises the proposed revisions to the net revenue tests proposed in Chapters 4 and 5.
- Chapter 7 details the proposals relating to the notification and pre-clearance of bundles containing Retail Fixed Narrowband Access. The chapter also details how unreasonable bundles are proposed to be modified or withdrawn.
- Chapter 8 details the proposed further specification of the obligation not to cause a margin/price squeeze in connection with the WPNIA market based on a Reasonably Efficient Operator ('REO').
- Chapter 9 questions whether the existing obligation not to cause a margin/price squeeze in connection with the market of Wholesale Broadband Access ('WBA') should be further specified to include the passing of a margin/price squeeze test similar to the net revenue test. The chapter also questions whether the D01/06 retail-minus price control should be amended from one based on a Similarly Efficient Operator ('SEO') to one based on an Equally Efficient Operator ('EEO').
- Chapter 10 details the obligations not to margin/price squeeze applicable to any potential future offer by Eircom of Naked WBA (Bitstream) DSL. It also proposes appropriate price floors based on a REO so that there is no margin/price squeeze to WPNIA.
- Annex A sets out the legal basis.
- Annex B sets out the Draft Directions that are proposed.
- Annex C provides ComReg's draft Regulatory Impact Assessment ('RIA') in relation to the Draft Directions.
- For information, Annex D details the consultation questions posed in Consultation Document No. 10/01 as well as a summary of the main views of respondents to that consultation.
- Annex E lists the questions asked in this consultation.

2 Executive Summary

2.1 The retail sale of telecommunication services by bundling more than one service together using the same bill and with typically one headline price has become the norm for most operators, be they fixed or mobile operators. Bundling has been generally welcomed by consumers as it reduces the number of bills they receive and can give some certainty on monthly spend where they keep their usage within their bundle's allowance. This trend has also seen many new entrants to the various markets, be they mobile operators into fixed, fixed into mobile and more recently content providers, such as cable, entering the retail broadband and telephony market.

2.2 Much of this is driven by consumer demand; however, in order to ensure all efficient players in the market can supply services at competitive prices to meet this demand, the regulator often has a key role.

2.3 The key regulated services in many Eircom bundles include retail fixed and wholesale narrowband access, wholesale voice (i.e. fixed origination and termination and mobile termination), WPNIA and WBA. The delivery of retail bundled services to end-users relies heavily on these key regulated inputs. This consultation and the annexed draft directions address the inter-relationship between these regulated inputs and sets out a proposed framework to ensure that potential anti-competitive behaviour by the Significant Market Power ('SMP') operator in one or more of these markets is mitigated through appropriate ex-ante controls. The key proposals of this consultation and draft directions are summarised below.

2.4 More recently OAOs have expressed an interest, based on expected consumer demand, in offering a retail stand alone broadband ("SAB") service. With this service, traditional PSTN voice is no longer supported and the access line is only used for broadband. This service may potentially prove to be popular with consumers that no longer use their landline for calls and who may opt for mobile only or voice over broadband as an add on to their broadband service. Given the expected introduction of SAB and its wholesale equivalent, "Naked" WBA DSL, ComReg considers it appropriate to provide clarity as to the treatment of regulated wholesale inputs within retail bundles that do not include retail fixed narrowband access (and which would no longer be subject to the obligation under Decision D07/61 not to unreasonably bundle). This consultation considers this in the context of the relevant underlying wholesale markets of WPNIA and WBA.

<u>Retail Fixed Narrowband Access:</u>

2.5 Pursuant to ComReg Decision D07/61[3], Eircom has an obligation not to unreasonably bundle retail fixed narrowband access with other retail services. The regulatory objective in this case is to prevent or mitigate the possibility of behaviour such as horizontal leveraging by the SMP operator from retail fixed narrowband access into other retail markets, as well as the maintenance/strengthening of a dominant position in the retail fixed narrowband access market itself. At present, the obligation not to unreasonably bundle services includes that Eircom, as the SMP operator, "*must ensure that any bundle avoids a margin squeeze and passes a net*

[3] 'Decision Notice and Decision Instrument - Designation of SMP and SMP Obligations Market Analysis: Retail Fixed Narrowband Access Markets' dated 24 August 2007

revenue test."[4] This consultation proposes to revise the current net revenue test so that the test remains appropriate and can be sufficiently responsive to the underlying competitive conditions that Eircom and OAOs may face over the forthcoming period.

2.6 Furthermore, significant operational issues and consumer detriment can arise where bundles are launched which subsequently do not comply with the regulatory obligation not to unreasonably bundle. Consequently, ComReg is also proposing – for the purposes of supporting the obligation not to unreasonably bundle – to further specify the pre-notification and pre-clearance requirements applicable to Eircom bundles that include retail fixed narrowband access. ComReg's preliminary view is that these further specifications strike an appropriate balance between the interests of consumers, Eircom and other operators.

Wholesale Physical Network Infrastructure ("WPNIA"):

2.7 The most important regulated products in this market are Local Loop Unbundling ("LLU")/Sub Loop Unbundling ("SLU") and Line Share. These are currently subject to a cost orientation obligation and are set at maximum prices of €12.41, €10.53 and €0.77 respectively following detailed consultations in recent years. With regard to the prices for LLU/SLU in particular, these are maximum prices and Eircom is free to reduce these prices, whether nationally or in certain areas, subject to competition law rules. To date the SLU product has seen no take up.

2.8 Eircom is currently subject to a regulatory obligation in the WPNIA market[5] not to cause a margin/price squeeze. This consultation will propose the further specification of this margin/price squeeze obligation by proposing a margin/price squeeze test based on a REO.

Wholesale Broadband Access ("WBA")

2.9 The supporting WBA market analysis which was recently completed (see Decision D06/11), noted the competition issues of leverage which a proposed WBA margin/price squeeze test would address. Therefore, ComReg is seeking views as to whether it is appropriate, as regards retail bundles that include WBA inputs, especially Naked WBA DSL, to further specify the WBA obligation not to margin/price squeeze to provide for a margin/price squeeze test (set out in more detail in Chapter 9). Subject to respondents' views and other relevant evidence, this possible further specification would be by separate direction.

2.10 This consultation also seeks views as to whether it is now, or might in future be, appropriate to change the retail-minus price control for WBA (as currently set out in Decision D01/06) from one based on a SEO[6] to one based on an EEO[7]. Using an

[4] At para 6.234 of ComReg Document No. 07/26 'Market Analysis: – Retail Fixed Narrowband Access Markets (Response to Consultation 06/39 and Consultation on Draft Decision)' dated 4 May 2007

[5] s.12.4 of ComReg Decision D05/10 dated 20 May 2010

[6] A SEO means an operator that shares the same basic cost function as Eircom but does not yet enjoy the same economies of scale and scope as Eircom – therefore it has a per unit cost higher than Eircom

EEO would result in lower retail costs being used in the net revenue test under Decision D07/61; consequently Eircom could pass these lower retail broadband costs as a lower price to its retail customers without cutting wholesale prices. ComReg is of the preliminary view that, based on its recent market review of the WBA market, the current condition of competition in Ireland does not warrant such a change although ComReg will consider all responses to this consultation and will continue to monitor other market evidence. If no change is made now, it may be reconsidered at a later date. In any event, ComReg will consult in 2012 on the possibility of a cost-based price control to set the maximum prices for WBA. It may consider then what, if any, margin test is appropriate in that context.

Preliminary views of this consultation:

2.11 In summary, having considered the views of respondents to Consultation Document No. 10/01, other relevant evidence, and any comments from the European Commission, and subject to the views of respondents to this consultation, the preliminary views of ComReg expressed in this consultation and draft directions are as follows:

Retail Fixed Narrowband Access:

2.12 It is ComReg's preliminary view that the application of the net revenue test under Decision D07/61, complemented by an assessment of the competitive context of the bundle in question, remains appropriate.

2.13 It is ComReg's preliminary view that the net revenue test should be sufficiently flexible to meet changes in competitive conditions. Therefore, subject to respondents' views and other relevant evidence, ComReg proposes the following further specification of the obligation not to unreasonably bundle under Decision D07/61, which would take effect when the resultant Direction becomes effective:

2.13.1 Currently, the net revenue test is based on a product-by-product assessment of each bundle. However, it is ComReg's preliminary view that this should now change to a two part test: Part 1 - an assessment of relevant portfolios of bundles on an Average Total Cost ("ATC") cost recovery basis; Part 2 - an assessment of individual bundles with a Long Run Incremental Cost ('LRIC') cost standard for retail calls. The cost standard for retail costs associated with Single Billing Wholesale Line Rental ("SB-WLR") and WBA should remain that as calculated under their respective retail-minus price controls. Therefore, until the price controls for SB-WLR and WBA are changed, the flexibility relating to individual bundles would relate only to the retail costs of retail calls. Changing the price control for SB-WLR and WBA would be by separate consultation.

2.13.2 In relation to setting the portfolios of bundles for Part 1 of the test, ComReg proposes, taking account of broad structural differences between areas, that

[7] An EEO means an operator that shares the same basic cost function as Eircom and has the same economies of scale and scope as Eircom

Eircom's current and future set of retail bundles can be categorised into one of the following possibilities:

- A: (1) Bundles sold from exchanges within the Larger Exchange Area; (2) Bundles sold from exchanges outside the Larger Exchange Area.

OR

- B: (1) Bundles sold from exchanges within the Larger Exchange Area; (2) Bundles sold from exchanges outside the Larger Exchange Area, (3) Voice only bundles

(Note: The proposed meaning of the Larger Exchange Area is discussed in detail in the paper and proposes to recognise that as different structural conditions can be increasingly observed, the possibilities for competitive and behavioural change may also potentially differ prospectively. In particular, ComReg proposes that the Larger Exchange Area reflects those areas where uptake of unbundled services, whether LLU and/or virtual unbundling in Next Generation Access ('NGA'), is likely to be viable.)

2.13.3 Currently, the net revenue test is based on historical ATC. It is ComReg's preliminary view that this measure of ATC could be allowed to reflect known future changes in wholesale costs and retail costs e.g. Mobile Termination Rate ("MTR") reductions. ComReg believes that this is an equitable approach and ensures that end-users immediately benefit from known future reductions to input costs. This would require retrospective monitoring to ensure that the cost reductions did, in fact, occur.

2.13.4 Currently, the net revenue test is based on 'resale' wholesale inputs (i.e. WBA (Bitstream) and SB-WLR). In other words, it is assumed that in order for a bundle to be replicable by an OAO that all OAOs use WLR and WBA exclusively. In order to reflect emergent use of LLU, ComReg proposes that this approach would remain only for bundles sold outside the Larger Exchange Area. For bundles sold within the Larger Exchange Area, a mechanism that reflects any emerging changes in competitive conditions of those urban areas may be necessary. One way to achieve this would be to calculate a wholesale input for the net revenue test by reference to the prices of WLR, WBA and LLU network input cost weighted for the relevant usage of each input by OAOs in the area. Because of the relatively low level of LLU penetration, the impact of this change at present would be modest. The idea however has the merit of reflecting emerging market conditions as a matter of course. Ultimately, if all, or nearly all, OAO activity in the relevant geographic footprint was over LLU, ComReg considers that it would not make sense to deny consumers the benefits of lower prices by maintaining retail prices commensurate with the more expensive WLR and WBA. This proposed approach would prevent this by applying a weighting of 100% to the LLU network input cost. In the meantime, it is proposed that this weighted average wholesale input be used in the net revenue test for bundles sold in the Larger Exchange Area.

2.13.5 In relation to unregulated products and services (e.g. mobile voice, mobile broadband etc), ComReg's main concern relates to Eircom's ability to strengthen its position in markets where it is dominant or where it has the ability to leverage its dominance by including unregulated products and services in a retail bundle of services below cost. Therefore, subject to respondents' views and other relevant evidence, ComReg proposes that unregulated services, such as mobile voice or IPTV, must cover their own LRIC. Additionally, in the case of mobile services, it is proposed that the aggregate of all the applicable unregulated products (i.e. all the mobile voice offers) must cover the Long Run Average Incremental Cost plus common costs ('LRAIC+') of the mobile voice service over the relevant network when it is included in a bundle of services that contain retail fixed narrowband access.

2.13.6 ComReg also proposes that there must be clear evidence that there has been no cross-subsidisation by Eircom between regulated markets and the markets for the unregulated products and services. It is proposed that such evidence will be gathered through periodic checks of business case models and/or review of the annual regulated accounts. On a case-by-case basis, ComReg could consider the use of Average Avoidable Costs ('AAC') for unregulated products and services where it is clear that competition in the market generally would not be harmed and that it would not create material distortions to competition through anti-competitive practices stemming from SMP products and services. Unlike the fixed network, currently ComReg has minimal up to date information on the likely LRIC / LRAIC+ costs of a mobile network in Ireland (although, pursuant to its powers under Decision D08/10[8], ComReg obtains separate accounts for Meteor and E-Mobile respectively which would aid in its monitoring of the costs). Therefore, the onus would be on Eircom to substantiate prior to launch that its unregulated product included in a bundled service meets the cost standard required. However, ComReg will also have due regard to the competitive context of the proposed bundling of the unregulated services and will be proportionate where it is clear that there will be no anti-competitive harm/foreclosure but that the proposed bundling is for the benefit of retail customers.

2.13.7 The proposals above can be represented graphically as follows:

[8] Response to Consultation Document No. 09/75 and Final Direction and Decision: Accounting Separation and Cost Accounting Review of Eircom Limited (Decision No. D08/10, Document No. 10/67, 31 August 2010).

	Current NRT	Proposed NRT
OAO modelled *(EEO/REO/SEO)*	EEO for calls and PSTN, SEO for BB	EEO for calls and PSTN, SEO for BB
Portfolio versus product-by-product	Product-by-product	ATC for portfolio / LRIC for retail calls in product-by-product
Cost standard *(ATC, LRIC…)*	ATC	
Relevant wholesale input *(WLR/WBA/LS+/LLU+)*	WLR + WBA	For Larger Exchange Area: Weighted average cost
Costs: Retrospective/ forward-looking	Retrospective	Forward-looking for known changes with retrospective monitoring
Unregulated products	Case-by-case assessment	LRIC (LRAIC+ for mobile network unregulated service as whole)

Figure 1: Preliminary views on possible revisions to net revenue test (NRT) applicable under Decision D07/61

<u>Possible future decisions in the markets of WBA and Retail Fixed Narrowband Access:</u>

2.14 Subject to respondents' views and other relevant evidence, ComReg is also seeking views on possible revisions to the retail-minus price control under Decision D01/06 and the net revenue test under Decision D07/61 that could be implemented by separate decisions at some later stage if competitive conditions warrant. ComReg is also seeking views as to whether the margin/price squeeze obligation in the WBA market should be further specified as set out in Chapter 9 below. Therefore, three future possible decisions/directions are as follows:

2.14.1 Revising the retail-minus price control for WBA under Decision D01/06 from SEO to EEO and therefore reflecting those EEO costs for broadband in the net revenue test under Decision D07/61 and the proposed margin/price squeeze test under Decision D06/11.

2.14.2 Dependent on increased take-up of LLU, replacing the proposed weighted average wholesale input cost in the Larger Exchange Area with the cost of Eircom's network in the relevant area, consistent with the calculation methodology for LLU prices. Therefore, the weighted average wholesale input proposal could be replaced by a LLU+ network input cost in Eircom's net revenue test as it would apply in the Larger Exchange Area. This use of a LLU+ network input cost, subject to respondents' views and other relevant evidence and competitive conditions, could be approximately one year from now in order to allow time for possible market developments and to allow OAOs sufficient time to revise their business strategy if necessary.

2.14.3 Further specifying the WBA obligation not to cause a margin/price squeeze (i.e. as set out in Decision D06/11) (dealt with in Chapter 9).

<u>WPNIA:</u>

2.15 ComReg is proposing the further specification of the margin/price squeeze obligation contained in Decision D05/10 such that the margin/price squeeze test would be based on a REO[9]. This is consistent with the approach proposed in Consultation Document No. 10/108 in relation to the minimum price for WBA by reference to a reasonably efficient LLU Line Share operator[10]; the draft decision included in Consultation Document No. 10/108 related to the modelling of the likely costs a REO operator might face when investing in/maintaining a broadband network. To ensure remedies imposed in the WPNIA market remain effective, ComReg believes it is critically important that there is sufficient economic space between wholesale products along the broadband value chain so that appropriate build/buy decisions can be made by OAOs. A decision on the appropriate WBA floors is due in the coming months following on from Consultation Document No. 10/108.

<u>Naked WBA DSL:</u>

2.16 In the near future, Eircom could offer Naked WBA DSL, as the wholesale equivalent of retail SAB/Naked DSL. Naked WBA DSL is a WBA product sold standalone without SB-WLR. This consultation confirms that the existing obligations not to margin/price squeeze in connection with the WBA and WPNIA markets would continue to apply to any offer by Eircom of Naked WBA DSL. ComReg considers that such a product offered by Eircom needs to recover the cost of Eircom's access network as Eircom is subject to an obligation of cost-orientation in respect of those access network costs. In this respect, the consultation proposes a floor for Naked WBA DSL that reflects the underlying access network costs in order to minimise the risk of a margin/price squeeze to WPNIA. The consultation also notes that any offer of Naked WBA DSL by Eircom will also be subject to the existing obligation not to margin/price squeeze in the WBA market pursuant to Decisions D01/06 and D06/11.

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[9] REO means a reasonably efficient operator which has a different basic cost function to Eircom and does not yet enjoy the same economies of scale and scope as Eircom. Therefore, its per unit costs would be higher than Eircom.

[10] Consultation Document No. 10/108 dated 22 December 2010

3 Background

3.1 ComReg's mission is to promote competition, foster innovation, and provide appropriate protection, for the benefit of all users of communications services[11].

3.2 ComReg's vision is to enable an environment in which:

3.2.1 Consumers, residential and business, are informed, empowered and protected and have a real choice of services at an affordable price.

3.2.2 A quality telecommunications service is available to all users and the availability and uptake of high speed broadband continues to be driven by cross-platform competition.

3.2.3 Investment and innovation are promoted through a responsive regulatory approach that instils a high level of confidence, certainty, consistency and transparency.

3.3 As the independent regulator for the communications sector, ComReg holds an important responsibility to deliver a transparent, predictable and stable regulatory environment and to foster the development of competitive electronic communications markets offering quality and choice for consumers, as well as promoting efficient investment and innovation.

3.4 This chapter provides some general background that respondents to this Consultation should be aware of in preparing and submitting their responses.

3.5 Eircom has been designated as the SMP operator in a number of upstream wholesale and downstream retail markets – in particular, the markets of Retail Fixed Narrowband Access (Market 1), WBA (Market 5) and WPNIA (Market 4). Therefore, Eircom is currently subject to a number of obligations, including price control as follows:

3.5.1 the obligation not to unreasonably bundle services in the Retail Fixed Narrowband Access market which includes not causing a margin squeeze and passing a net revenue test

3.5.2 the obligation not to cause a margin/price squeeze in connection with the WBA market

3.5.3 the obligation not to cause a margin/price squeeze in connection with the WPNIA market

3.6 The purpose of such obligations is to ensure that Eircom, as a vertically integrated operator and with SMP, acting as both a retail operator and as a wholesale provider of services to both infrastructure based OAOs and OAOs that simply rely on a resale of Eircom's wholesale inputs, does not act anti-competitively. To achieve ComReg's regulatory objective of promoting efficient investment and protecting the interests of end users, it is important to ensure that there are appropriate protections and incentives in place for OAOs who choose to climb the ladder of investment as opposed to acting as resellers. These are set out below:

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[11] Document No. 10/47 'ComReg's Strategy Statement 2010 – 2012' dated 1 July 2010. See also ComReg's objectives as set out in section 12 of the Communications Regulation Act 2002

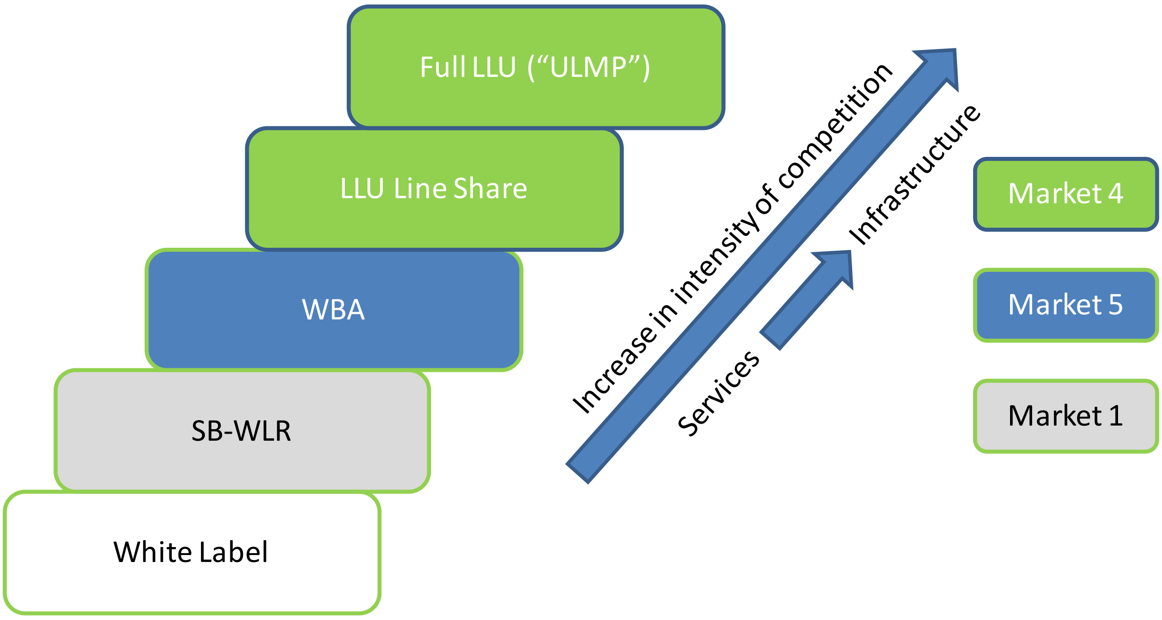

Figure 2: Ladder of investment

3.7 As the European Commission has noted:

"*Competing network infrastructures are essential for achieving sustainable competition in networks and services in the long run.*"[12]

3.8 Appropriate protection and incentives will enable OAOs to climb this investment ladder by ensuring that Eircom cannot squeeze between the relative prices of its different wholesale products across and within regulated markets. For example, Eircom's price for SB-WLR and WBA combined should always be greater than its price for SB-WLR and LLU Line Share ("LS") combined which in turn should always be greater than its price for Full LLU ("ULMP"). This can be represented graphically as follows — which demonstrates how an OAO's greater investment in infrastructure based wholesale products will result in a reduced recurring monthly wholesale input cost per month for the OAO:

[12] Explanatory note accompanying Recommendation on relevant Product and Service Markets, C(2007) 5406

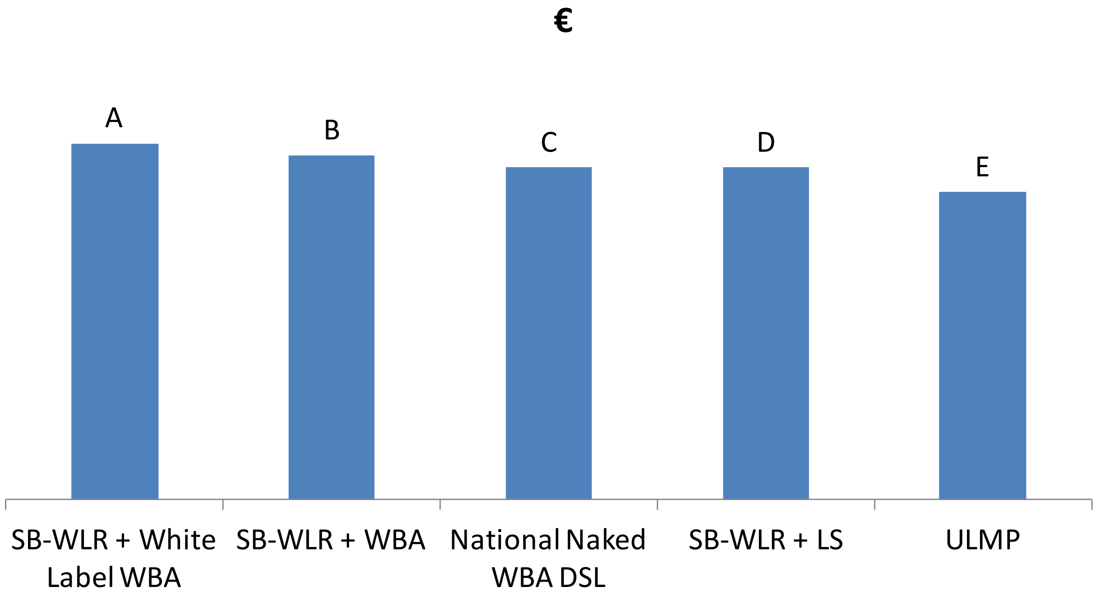

Figure 3: Reduced monthly wholesale input cost for OAOs as they climb ladder of investment

3.9 ComReg considers that infrastructure based competition from OAOs using LLU ("LLUOs") has the most potential to offer sustainable competition to Eircom in the provision of broadband to the benefit of customers. In general, LLUOs are better able to offer differentiated retail products and to set prices independently of Eircom as compared to those OAOs using WBA and WLR. Consequently, it could be in Eircom's interests to set, say, WBA prices low enough to discourage investment in LLU / ULMP even where alternative investment is viable. Therefore, it is important that regulation ensures that LLU based competition is encouraged where it is viable. This may require constraints on Eircom in the short run. Ultimately as LLU becomes more prevalent and LLUOs attain greater economies of scale ComReg considers that it should be possible then to relax some of these constraints. From the perspective of consumers there is likely to be a trade off against the short term ability of Eircom to price cheaply against a longer term benefit of effective competition with consequent lower prices and greater choice over the medium term.

3.10 ComReg considers that competition in the provision of retail services is heavily dependent on effective competition at the wholesale level, or, where this is not the case, through regulation of the applicable wholesale markets. This is why ComReg is proposing in this consultation to clarify certain obligations in wholesale markets as well as revisiting the regulation of retail fixed narrowband access. Even if all retail markets were to become competitive the concerns about leverage from regulated wholesale markets would persist.

3.11 The Irish telecommunications sector is changing and both Eircom and the OAOs are facing an increasing potential for localised competitive pressures to emerge at retail level. One of the most fundamental structural changes to the fixed broadband market that has taken place over the past eighteen months has been the upgrade of cable networks in urban areas. ComReg's recent review of the WBA market review has found evidence of structural change arising in certain overlapping geographic areas. This was identified as being relatively recent and not yet sufficiently stable to conclude sub-national geographic markets.[13] However, should such structural change facilitate behavioural change in the future, consumers should ultimately reap the benefits of higher broadband speeds at more competitive prices. With this structural change comes the challenge of ensuring that the long term competitive dynamics of the market are not distorted and all operators relying on Eircom's network, including Eircom itself, are not unduly hindered in their efforts either by Eircom's dominant position, or in Eircom's case, by regulation.

3.12 ComReg considers that retail competitive pressures may prospectively differ by geographic area subject to the underlying structural characteristics and investment incentives/viability. Such possible variations and can be broadly represented graphically as follows:

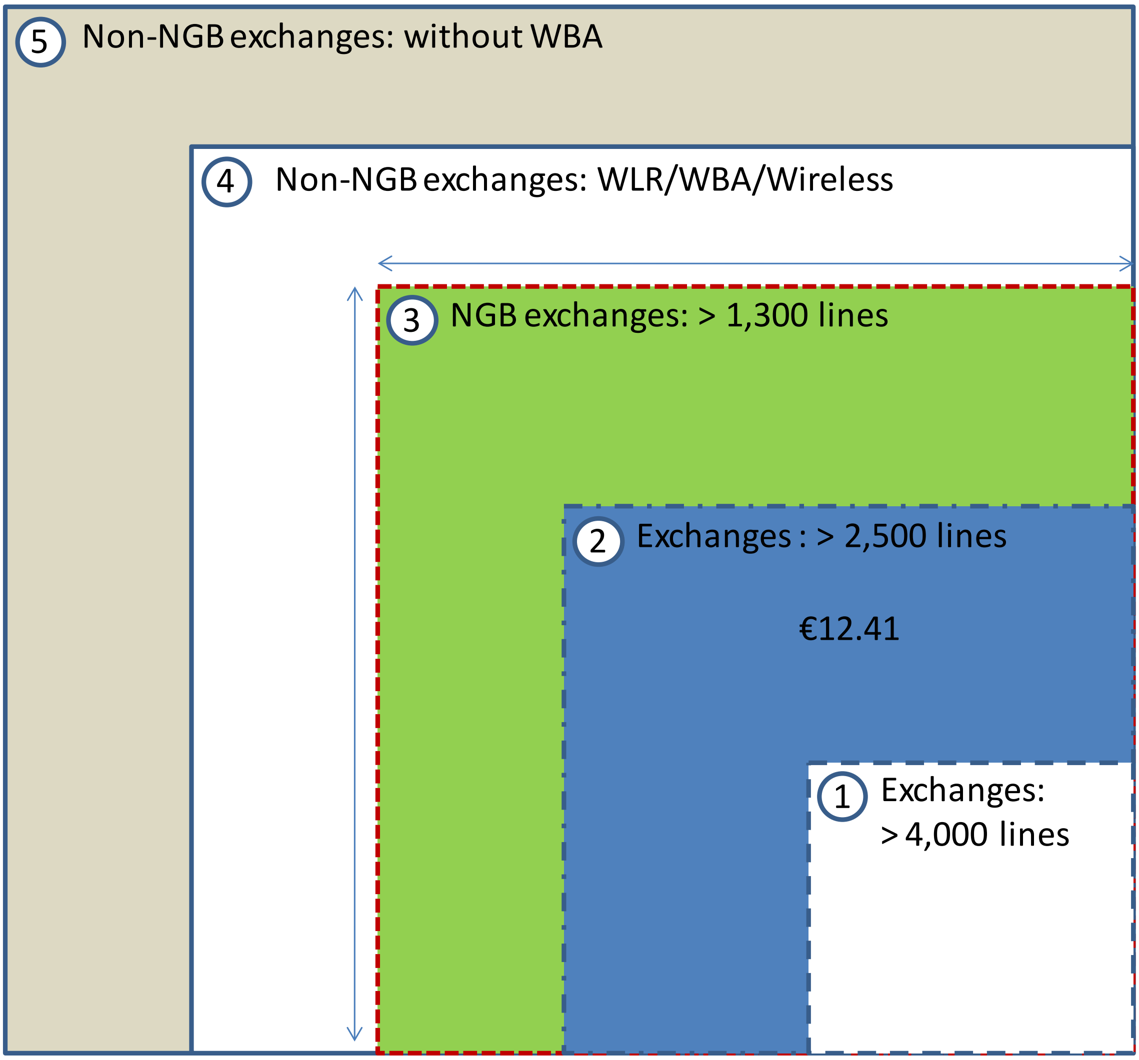

Figure 4: Geographic areas of platform availability – used as cross reference diagram to explain proposed revisions to the net revenue test

[13] ComReg Document 11/49, Market Review: Wholesale Broadband Access, Response to Consultation and Decision, Decision No. D06/11, 08 July 2011.

3.13 In the above:

- "Area 1" represents the current footprint of LLU which ComReg believes, for the most part, also matches the current footprint of UPC[14]. This is estimated to be c.80-90 exchanges. This area is likely to be made up of densely populated urban areas with the highest number of access lines per exchange.
- "Area 2" represents the potential footprint of LLU that was assumed in order to set the maximum price of ULMP at €12.41 per month. However, actual LLU take-up has been low in this area. In 2008 and 2009, ComReg built a cost model for all Areas above based on a Bottom Up Long Run Average Incremental Cost ("BU-LRAIC") basis in order to derive a price for LLU. In ComReg Decision D01/10, a maximum price of €12.41 per month per line was established. This was on the assumption that only 149 of the largest exchanges (i.e. those with more than 2,500 connections) would ever be unbundled. As stated earlier, to date, only approximately 80-90 exchanges have in fact been unbundled which would indicate that the ULMP price as currently charged by Eircom to OAOs may be in excess of the cost of associated with the currently unbundled exchanges. It is clear that if Eircom wishes to improve the competitiveness of its network it could do so without any regulatory difficulties simply by cutting the price of LLU. This is a matter that ComReg will keep under review.
- "Area 3" represents the footprint of Eircom's Next Generation Broadband ('NGB') where Eircom offers "uncongested" broadband to its retail and wholesale customers. This is c.250 exchanges situated across the country.
- "Area 4" represents the footprint of Eircom's non-NGB WBA.
- "Area 5" represents the area with no broadband provision by Eircom and relates to mainly very rural areas (there may be broadband through the National Broadband Scheme/other fixed/mobile wireless providers in this area).

3.14 Figure 4 above indicates that while regulation may be justified across the national territory its emphasis may vary geographically due to the underlying structural characteristics. In Area 1 and also possibly Area 2 ComReg will be concerned to encourage LLU while it is still nascent and to avoid placing the Eircom platform as a whole at an unfair disadvantage against cable. Structural conditions probably mean that excessive pricing by Eircom at a retail level may become less of a concern. ComReg also believes that it is important to set out how regulatory constraints on Eircom may evolve if competition over LLU becomes more entrenched.

3.15 In Areas 4 and 5 it appears clear that LLU nor cable based competition will never be significant factors. Here indirect access services such as WLR and WBA will be the only means of providing an alternative to Eircom – at least over fixed platforms. Here it will be important to ensure that these services are viable and also to guard against excessive pricing.

[14] Analysis suggests that the current cable footprint matches c.100 of Eircom's exchanges and per UPC publicly available data, UPC broadband is currently available to c.700k residential addresses. Latest publicly available customer numbers for UPC are 224,800 broadband customers and 121,200 phone connections.

3.16 Area 3 represents those areas where neither cable nor LLU based competition are likely but where it has proven possible for Eircom to upgrade its core network to allow it to offer what it calls Next Generation Broadband ("NGB") at the retail level and Bitstream Managed Backhaul ("BMB") at the wholesale level i.e. its "uncongested" up to 8 mb/s and 24 mb/s broadband products. Significantly, this is also likely to correspond fairly closely to Eircom's ultimate footprint for NGA services i.e. those based on the proposed fibre optic upgrade to the access network[15].

3.17 On the face of it, it would seem appropriate not to include Area 3 in the Larger Exchange Area because of the lack of LLU or cable. On the other hand if NGA roll out does take place and if Eircom were to offer an acceptable unbundling product at wholesale level that was viable across this footprint, ComReg considers that Area 3 could be categorised in a similar manner to Areas 1 and 2: if not now, then as soon as industry and ComReg had more clarity in respect of NGA roll out.

3.18 The significance of this discussion is whether in future – when LLU has become widespread - Eircom's wholesale cost input for the purpose of the net revenue test at the retail level should be assumed to be that of a nationally averaged WLR/WBA service or a more regionally based input cost analogous to the LLU price. It is ComReg's provisional view that maintaining retail prices artificially high in the long term may render Eircom unfairly uncompetitive and deny consumers in these areas the benefits of lower prices.

3.19 The significance of this discussion also manifests itself below in the context of designing an appropriate wholesale input cost for use in the net revenue test of Decision D07/61 and the possible margin/price squeeze test which may potentially be further specified under Decision D06/11.

Considerations to balance in this consultation:

3.20 The key issues outlined above are the main considerations of this consultation — to inform ComReg's decision making and ensure a considered decision which achieves a balance that:

3.20.1 Allows Eircom to compete with any emergent infrastructure competition to the benefit of end-users;

3.20.2 Allows efficient OAOs using Eircom's key regulated inputs to compete which, as shown in the supporting market analyses, continues to be to the benefit of end-users;

3.20.3 Ensures appropriate incentives remain for both Eircom and OAOs to invest efficiently in broadband infrastructure;

3.20.4 Ensures efficient OAOs are not squeezed to the point where they are forced to exit to the ultimate detriment of end-users; and

3.20.5 Ensures that retail end-users can benefit from competitive bundle options.

3.21 If, subject to respondents' views and other evidence, ComReg allows Eircom a different treatment of bundles in areas where structural characteristics could lead to

15 http://pressroom.eircom.net/press_releases/article/eircom_announces_locations_for_phase_1_fibre_rollout/

prospectively more competition, defining this area is an important consideration of this consultation. Based on considerations outlined above it seems to ComReg that Areas 1 and 2 of Figure 4 have the potential for LLU based competition. However, it is less clear that Area 3 (where Eircom's NGB services are available) meet this criterion. ComReg considers that an important consideration in this respect is whether Eircom's proposed NGA roll out and its proposal to offer virtual unbundling may make unbundled solutions more viable in Area 3. If this is the case, Area 3 may be a more appropriate footprint against which to assess the impact of infrastructure based competition. ComReg intends to set out its preliminary views in respect of NGA related matters in a separate consultation and will have regard to that NGA consultation in a final decision on this paper.

3.22 Therefore, ComReg proposes to set a 'Larger Exchange Area' to recognise that as different structural conditions are considered present, the possibilities for competitive and behavioural change may also differ prospectively. In particular, ComReg proposes that the Larger Exchange Area reflects those areas where uptake of unbundled services, whether LLU and/or virtual unbundling in NGA, is likely to be viable and where regulation should be responsive to any prospective changes. Areas outside the Larger Exchange will be referred to as the "Smaller Exchange Area". Based on respondents' views and other relevant evidence, the Larger Exchange Area could be set to cover Areas 1 and 2 only of Figure 4, or it could be set to cover Areas 1 – 3 of Figure 4.

3.23 In particular, the above impacts on ComReg's proposals in relation to:

3.23.1 Assessing the revised net revenue test under D07/61 / possible margin/price squeeze test of D06/11 by formulating portfolios of certain bundles together based on whether they are sold within or outside the Larger Exchange Area.

3.23.2 The applicable wholesale input cost for bundles under the revised net revenue test under D07/61 / possible margin/price squeeze test of D06/11 based on whether they are sold within or outside the Larger Exchange Area.

3.24 This consultation and draft Directions consider all of the above in the following sections under the relevant markets. These considerations should be kept in mind by respondents in answering the questions to this consultation.

4 Obligation not to "unreasonably bundle" in the Retail Fixed Narrowband Access markets: proposed further specification of the net revenue test

Background

4.1 The purpose of this chapter is to seek views on whether the obligation under Decision D07/61 not to unreasonably bundle services should be further specified or whether the current net revenue test remains appropriate — given the regulatory objectives of the obligation not to unreasonably bundle set out in Consultation Document No. 07/26[16]. The net revenue test is an ex-ante imputation test to assess whether a bundle offered by Eircom is above an appropriate level of cost and is one test to assess whether a bundle is reasonable. The current net revenue test uses ATC and the test is conducted on a bundled product by bundled product basis, an example being Talktime Chatter with 8Mb broadband. Subject to respondents' views and other relevant evidence, ComReg is proposing a modified specification of the net revenue test from that currently applied.

4.2 The consultation is also seeking views on a further specification of the current obligation as regards the pre-notification, pre-clearance, modification and withdrawal of bundles that include retail fixed narrowband access, pursuant to Regulation 13 of the Universal Service Regulations[17] and ComReg Decision D07/61. This is examined in Chapter 7.

4.3 Following a detailed market review of the Retail Fixed Narrowband Access markets in 2007, ComReg found Eircom to have SMP in those markets. A new market review of Retail Fixed Narrowband Access has commenced and ComReg expects to publish an initial consultation in 2012. However, this process will not be complete for some time. ComReg is proceeding with the current consultation under the current market review. ComReg believes that there is an urgent need to ensure that regulation remains relevant and proportionate so that the net revenue test takes account of any differing structural conditions which could potentially support the emergence of more localised competitive pressures at the retail level over time. The proposed changes are designed so as not to pre-empt or deter any such developments but rather to ensure that regulation can be sufficiently responsive if they occur.

Possible benefits of bundles

4.4 It is important to note at the outset that ComReg recognises that bundling can be inherently efficiency-enhancing and can help promote competition and deliver important benefits to consumers. In particular, bundling multiple services into one overall package can be an effective means for communications providers to realise production, transaction, marketing and distribution efficiencies, pass on cost savings to consumers, expand market demand, etc.

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[16] 'Market Analysis: – Retail Fixed Narrowband Access Markets (Response to Consultation 06/39 and Consultation on Draft Decision)' dated 4 May 2007

[17] European Communities (Electronic Communications Networks and Services) (Universal Service and Users' Rights) Regulations 2011

4.5 As noted by ComReg in paragraph 6.135 of Consultation Document No. 06/39[18]:

"*ComReg acknowledges that the bundling of end-user services can be, and usually is, welfare-enhancing. Bundling is not anti-competitive per se, and indeed may generate significant efficiencies for consumers, e.g., in terms of lower prices, increased choice, lower transaction costs, etc. Consumers may value receiving multiple services from one provider and with only one bill. Also, the price of a bundle will generally be less than buying the elements individually, and this price may simply reflect productive efficiencies that should be encouraged.*"

4.6 However, as noted by ComReg in the following paragraph of that consultation, "*bundling can have some negative consequences*" and, in the light of Eircom's SMP in a number of important input markets, those reasons are the regulatory objectives of the obligation not to unreasonably bundle. Those potential negative consequences are further elaborated below.

Obligation not to unreasonably bundle

4.7 As part of the 2007 market analysis process certain remedies were imposed on Eircom. One of the remedies was that it shall not unreasonably bundle retail fixed narrowband access with other services. ComReg set out what would be considered as unreasonable bundling in Consultation Document No. 07/26 which is construed together with ComReg Decision 07/61[19.] To ensure that Eircom would not unreasonably bundle, the following requirements were specifically noted in Consultation Document No. 07/26:

4.7.1 Eircom must offer all retail narrowband access services as standalone products;

4.7.2 Eircom must not price a retail bundle, which includes retail narrowband access, at a price which is below the costs of the fixed wholesale regulated elements; and

4.7.3 Eircom must ensure that any bundle avoids a margin squeeze and passes a net revenue test[20]. Furthermore, pending a final Decision being in effect following the current consultation a settlement agreement between Eircom and ComReg in relation to the net revenue test remains in effect[21].

The competition problem: reasoning for the net revenue test

4.8 As noted in Consultation Document No. 10/01, given the existence of a dominant operator in the retail fixed narrowband market, the objective of the obligation not to unreasonably bundle was to facilitate the development of effective competition and to mitigate against the risk of the SMP operator leveraging into closely related

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[18] 'Market Analysis: – Retail Narrowband Access Markets' dated 17 August 2006

[19] See 1.1v of the Decision Instrument in ComReg Decision D07/61

[20] The net revenue test is an ex-ante test and is synonymous with the term "imputation test".. Details of the current net revenue test can be found in ComReg Information Notice 09/08

[21] See ComReg Information Notice 09/79 dated 14 October 2009 @ http://www.comreg.ie/_fileupload/publications/ComReg0979.pdf

markets — thereby reinforcing its dominance in the market for retail fixed narrowband access.

4.9 As noted in paragraph 6.229 of Consultation Document No. 07/26: "*ComReg does not believe that the application of competition law alone would adequately address potential market failures. … As set out above, as a vertically integrated undertaking, the SMP operator may have the incentive to leverage its market power. ComReg believes that it is the appropriate body to monitor and if necessary intervene in a timely manner, because of its expertise in the market and the overlap with other retail obligations in the retail narrowband access markets …*"

4.10 The European Regulators' Group ('ERG') of telecommunications authorities also makes the same point in its report on margin squeeze:

"*These objectives as laid out in Article 8 of the Framework Directive are to: 'promote competition (…), contribute to the development of the internal market (…), promote the interests of the citizens of the European Union.' While competition law is intended to prevent margin squeeze as an exclusionary abuse, ex-ante regulation seeks the more ambitious goal of promoting competition by facilitating entry into those markets.*"[22]

4.11 As such, ComReg considered that the ex-post enforcement provided under competition law would be inadequate and consequently considered that the express condition of imposing ex-ante regulation, as is the case of the unreasonable bundling obligation, would be more appropriate. Furthermore, given the identified risk of potential leverage arising from Eircom's SMP in important input markets, it is further considered that identifying unreasonable bundling only after it has occurred would not sufficiently protect against possible market foreclosure and the associated consumer harm.

4.12 Consultation Document No. 07/26 is particularly relevant in the context of the unreasonable bundling obligation. As indicated in footnote 40 of ComReg Decision D07/61, the obligation is to be construed in the light of the reasoning in Consultation Document No. 07/26. Consultation Document No. 07/26 sets out in considerable detail the analysis of the basis for and content of the SMP obligation not to unreasonably bundle. In particular:

(1) Paragraph 6.218 explains the detailed competition concerns in the case of bundling practices:
"*…There may be the potential for operators, notably dominant operators, to leverage strong market and branding positions and to use bundling strategies for anti-competitive reasons. This may allow an operator already dominant in one market to leverage its dominance into closely related markets. Bundling could also be used to potentially protect and indeed enhance a position of dominance in the retail narrowband access markets. The inability of new entrants to compete profitably with the dominant operator's bundled offerings may increase entry barriers in these markets. For instance, eircom might offer access bundled with a package of free, or heavily discounted, call minutes (including both fixed and mobile calls). In that context, and where alternative suppliers were constrained in offering the same kind of bundles as the incumbent operator, the bundling of retail products could*

[22] ERG (09) 07 Report On the Discussion Of The Application Of Margin Squeeze Tests To Bundles, para. 6

potentially distort competition by leveraging into closely related markets and by distorting pricing in such markets…"

(2) Paragraph 6.219 sets out the concern about competitors' ability to profitably replicate Eircom's bundled pricing:

"There is nonetheless a risk that eircom may induce a margin squeeze through bundled pricing. This occurs when equally, or more, efficient operators are unable to profitably replicate eircom's bundled offering, and are effectively foreclosed from competing with eircom in respect of its bundled products. For example, if eircom were to apply a margin squeeze in respect of the retail narrowband access element of a bundled offering this may undermine the effectiveness of the mandated wholesale inputs since OAOs may not be able to effectively replicate the access element of that bundle (due to an insufficient margin). Should eircom engage in such behaviour it could have the effect of i) reinforcing its dominance in the retail narrowband access markets and / or ii) leveraging that dominance into related markets due to an inability on the part of OAOs to effectively replicate the access part of the bundle."

(3) Paragraph 6.232 then concludes on the core regulatory concern in relation to retail bundling, i.e., reinforcing Eircom's SMP in retail narrowband and leveraging that SMP into other related markets:

"*However, there is a need for some obligation to prevent bundling being used for anti-competitive purposes, in particular where it may be used to disguise a possible margin squeeze in respect of the retail narrowband access element of the bundle and thereby potentially reinforce eircom's dominance in the retail narrowband access markets and providing scope for leveraging into related markets.*"

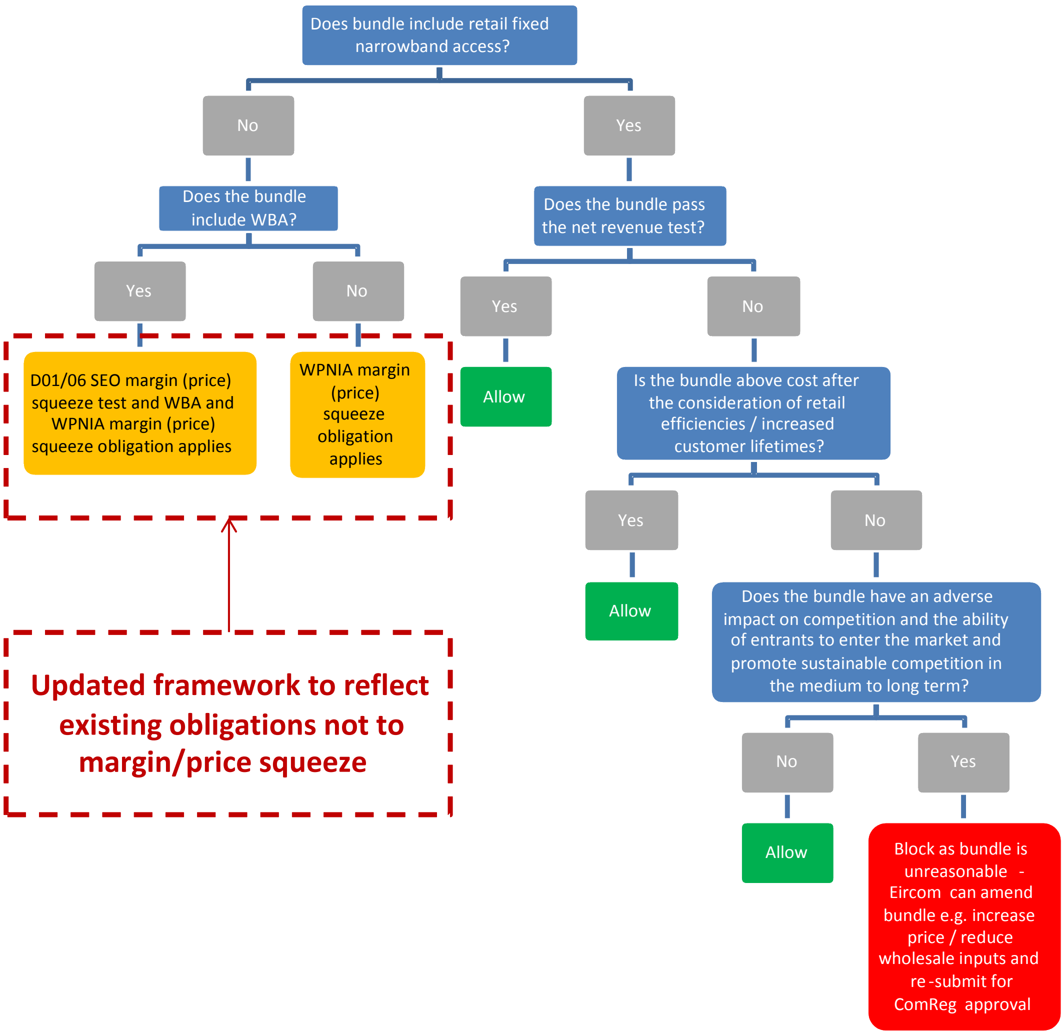
4.13 Without the net revenue test, Eircom could cause a margin squeeze against OAOs by pricing its bundles anti-competitively. If this occurred, OAOs would have to attempt to match Eircom's anti-competitive pricing in order to stay in the markets of Retail Fixed Narrowband Access. However, with a continued squeeze, this would ultimately lead to OAOs' exit and entrants not being encouraged to enter as their costs would not be covered over the long-term This would ultimately be to the detriment of consumers as absent any competition, Eircom could then raise the prices of its retail fixed narrowband access bundles in most geographic areas. This could re-inforce Eircom's SMP position in large sections of the country where the likelihood of competition expanding would be significantly reduced, which would not be in the interests of those consumers in those areas.

4.14 The obligation not to unreasonably bundle specified that Eircom "*must ensure that any bundle avoids a margin squeeze and passes a net revenue test*" in order to ensure that the problems above do not arise.

Avoiding a margin squeeze and passing a net revenue test

4.15 This part of the consultation concerns the requirement on Eircom to avoid a margin squeeze and to pass a net revenue test for its bundles that include retail fixed narrowband access. Additionally, where bundles do not include retail fixed narrowband access but do include WBA, the existing SEO margin (price) squeeze test of D01/06 applies. This is re-enforced by Decision D06/11 in relation to WBA which imposes an obligation on Eircom not to cause a margin/price squeeze. Since Decision D05/10, an obligation also falls on Eircom to not to cause a margin/price squeeze in connection with the market for WPNIA. These two additional points were added to the framework for analysis and are highlighted below for clarity.

Figure 5: Current framework to assess bundles updated to reflect existing regulatory obligations to not margin/price squeeze



Introducing possible revisions to the current net revenue test

4.16 Over the past eighteen months there have been certain changes in structural conditions with the upgrade of networks in predominantly urban areas. Furthermore, Eircom together with the other fixed operators utilising wholesale inputs from Eircom have faced a growing presence of alternative infrastructure operators such as the cable operator UPC. While the prospect of more localised competitive pressures at the retail level does not yet appear to have translated into a sub-national pricing/marketing response, ComReg is mindful to ensure that the long term competitive dynamics of the market are not distorted through regulation and that all operators relying on Eircom's network can compete effectively where appropriate. Therefore, ComReg believes that there may be merit in revising the parameters of the net revenue test to ensure it can be sufficiently responsive if relevant competitive developments occur.

4.17 However, ComReg considers that the assessment of whether, and under what circumstances, the net revenue test could be revised would need to recognise the objectives that are central to ex-ante regulation. More specifically, ComReg considers that there are a number of reasons why careful consideration should be exercised before revising the current net revenue test. These include:

4.17.1 Ex-ante regulation should provide efficient entrants with wholesale prices that are viable and are not subject to uncertainty. Any undue flexibility provided to Eircom could force entrants onto a loss-making price trajectory that is not sustainable in the long run. This would not be consistent with the regulatory objective of promoting effective competition.

4.17.2 Eircom continues to have a strong position in the regulated markets of Retail Fixed Narrowband Access, Call Origination, WPNIA and WBA. These focal products included in bundles are not new or emerging products.

4.17.3 While some OAOs are currently providing bundles with lower prices than Eircom, evidence of OAOs undercutting Eircom at a certain point in time is not sufficient to support the conclusion that Eircom should be allowed to reduce its prices to a level that would be below relevant costs. First, entrants may need to undercut the incumbent's prices by an amount equivalent to the end-customers' perceived cost of switching providers. Second, incumbents tend to have well-established brands on the supply of all of the services included in the bundle, which it may not be possible to replicate with short-term marketing expenditure. Third, entrants may need to invest in the short-term (by pricing at a loss) in order to gain sufficient market share to achieve the economies of scale that would enable them to operate profitably in the long run.

4.18 The extent and impact of any emergent inter-platform competition from competitors such as UPC also needs careful consideration to ensure any regulatory framework in place does not distort the ability of one network to compete over another and give an unfair advantage to any one network.

The current net revenue test

4.19 The current net revenue test (conducted on a per month basis for each individual bundle) consists of the following for all bundles that include retail fixed narrowband access (retail line rental) launched by Eircom as SMP operator in the retail fixed narrowband access market. As set out publicly in Information Notice No. 09/08, the current net revenue test is as follows:

Figure 6: Current net revenue test as extracted from Information Notice 09/08

NET REVENUE TEST (all ex VAT)	**Factors considered in the net revenue test**	**DISCUSSED IN THIS CONSULTATION AS:**
Revenue:		COMPONENT ONE *(see paragraph 4.35)*
Package Price	This is the bundle package price charged to retail customers.	
Calls Revenue	This is the total calls revenue earned on average outside the bundle package. This is calculated for each component that is charged separately outside the bundle by: (i) taking the total calls for that component and multiplying that by the call set up fee; and (ii) taking the total minutes for that component and multiplying that by the retail price per minute. This total revenue for the component is then divided by the total number of customers to get average revenue per customer for that component. The totals of all revenue components sold outside the bundle are included.	
Costs:		
Wholesale line rental	This is the Single Billing –Wholesale Line Rental regulated price as per the regulated retail minus price control and as published in Eircom's Reference Interconnect Offer price list.	COMPONENT TWO *(see Chapter 5)*
Operating costs associated with retail line rental	These are the operating costs as derived from the SB-WLR regulated retail minus price control. *Therefore, the full cost of retail line rental, that is the SB-WLR plus the associated retail costs as per the regulated retail minus price control, is taken into account in the analysis.*	COMPONENT THREE *(see paragraphs 4.37-4.38)*
Mailbox	Where the bundle packages include free mailbox, the wholesale price of the mailbox as per the regulated retail minus price control as published in Eircom's Reference Interconnect Offer Price List must be taken to ensure an operator can replicate the offer. However, consideration will be taken of the take up of the mailbox and the wholesale price will be adjusted to reflect this. The retail costs as derived from the retail minus price control could also be included here.	COMPONENT SIX (*see paragraph 4.80*)
Costs associated with retail calls	These are the wholesale and retail costs as calculated for each retail cost, e.g. calls to Local, National, UK etc. The retail costs of each are calculated by including the wholesale interconnection prices applicable in the market plus the latest audited average total retail costs (residential average total costs for a residential bundle, business average total cost for a business bundle) provided by Eircom and as reviewed and approved by ComReg. Where applicable, these total retail costs include relevant international calls out payments costs and mobile termination costs applicable (including the costs and mobile termination costs for those mobile calls that are sold for free).	COMPONENT FOUR *(see paragraphs 4.40-4.69)*
Wholesale broadband	This is the relevant regulated WBA price as per the regulated retail minus control and as published in Eircom's Bitstream price list.	COMPONENT TWO
Operating costs associated with retail broadband	These are the operating costs as derived from the WBA regulated retail minus price control.	COMPONENT THREE
Net Revenue: Total Revenue – Total Costs	***If total costs are greater than total revenue, bundle is not profitable***	

If the above results show the costs are above revenue, ComReg, as a proportionate measure, will consider any robust evidence of retail efficiencies or increased customer lifetimes as a result of bundling to assess against the loss of the bundle. ComReg will also consider the impact on competition and the ability of entrants to enter the market and promote sustainable competition in the medium to long term.

Possible revisions to the current net revenue test

4.20 The proposed revised net revenue test has three steps:

- Step One: Currently, this step involves identifying the individual bundle to be assessed. However, in the below in paras 4.21 – 4.33, ComReg is seeking views as to whether the test should assess bundles on a product by product basis or on a portfolio basis or combination of both.
- Step Two: This involves conducting the net revenue test. Currently, the components of the net revenue test are the same for all bundles. However, in this consultation, ComReg is seeking views as to whether the net revenue test should be revised to consider:
  - A different treatment of bundles in the Larger Exchange Area
  - Use of EEO costs for WBA retail costs as compared to using SEO costs
  - Some other measure of cost as against the use of ATC.
- Step Three: This involves a case-by-case assessment of the likely impact of the bundle on competition if the relevant cost is not covered. ComReg proposes that this step should remain.

STEP ONE: PORTFOLIO / PRODUCT BY PRODUCT ASSESSMENT APPROACH

4.21 Currently, the net revenue test applies to individual bundles and not to any aggregation of bundles. For example, the test applies to the ‘1MB TalkTime Anytime’ bundle and not to the whole ‘Anytime’ bundle range offered by Eircom as SMP operator in the market for retail fixed narrowband access.

4.22 ComReg considers that there are a number of reasons underpinning the use of a product-by-product test in an ex-ante setting, which are consistent with the regulatory objective to provide entry assistance for efficient entrants to markets where Eircom has SMP.

4.22.1 It may not be realistic to require a new entrant to replicate all, or a large part, of Eircom’s product mix or, at the extreme, its entire product portfolio.

4.22.2 Carrying out the margin squeeze analysis at the individual product level provides for a range of competitive outcomes. Conducting the test on an aggregate basis requires ComReg to specify the products included in the portfolio which can prove challenging in practice.

4.22.3 A product-by-product test approach may be appropriate when there might be “*a new offer giving rise to a margin squeeze, which is currently subsidised by other profitable offers but whose volumes could increase substantially in the future, subsequently leading to an overall negative margin in the future.*”[23]

[23] European Commission (2007), ‘Wanadoo España vs. Telefónica’, Case COMP/38.784, paragraph 387, p.109.

4.23 However, from an economic perspective, ComReg recognises that there are efficiency gains that could be achieved through a portfolio assessment approach:

4.23.1 A welfare-maximising pricing structure of a multi-product firm with market power is one where common costs are recovered such that there is an inverse relationship between prices and elasticities of demand. Thus, in a static sense, this would suggest that as long as the overall portfolio passes the net revenue test the aggregate approach would be beneficial for consumer welfare.

4.23.2 As an entrant gains market shares, its decision-making process entails an assessment of the profitability of its investment over the entire range of products it will offer in the market — which suggests that the aggregate test should be applied.

4.24 Furthermore, ComReg considers that a review of OAOs' retail bundled offers shows that OAOs do offer broad portfolios of services, rather than focusing on a particular product specification, or indeed a narrow customer segment generally.

4.25 A possible way forward which combines the advantages of both approaches might be to apply a test both at a portfolio level and at an individual product level. This might entail applying a test based on ATC to the portfolio while also insisting that each product within the portfolio covers a lower cost standard:

4.25.1 Part One: Test is applied at portfolio level which aggregates certain individual bundles together. However, careful consideration must be given to how these portfolios are ascertained and this is discussed below.

4.25.2 Part Two: Test is applied at individual bundle level with a lower cost standard for retail calls in the bundle. This cost standard may apply later for retail broadband costs also, if respondents' views and other relevant evidence, supports a move to EEO for those retail costs. The individual bundle assessment will always be subject to the proviso that the aggregate of bundles (Part One of the test) passes ATC. The precise nature of this lower cost standard is discussed later in this chapter.

Proposal: To revise the net revenue test to a two-part test: Part 1) Portfolio aggregate bundle assessment based on ATC and Part 2) Individual bundle assessment with lower cost standard required for retail costs associated with calls.

How to ascertain the portfolios of bundles?

4.26 ComReg believes that the definition of portfolios should recognise the demand and supply conditions of individual bundles — and the grouping of certain individual bundles should be conducted by identifying those bundles that are considered broadly substitutable. ComReg's key concern is whether the pricing behaviour of the dominant operator, Eircom, is likely to exclude efficient operators or at least restrict their ability to compete effectively in the Retail Fixed Narrowband Access and related markets.

4.27 Consequently, to ascertain the portfolios of bundles, ComReg considers a practical and robust view would be required recognising the following attributes:

- Bundles included in the portfolio are considered as relatively close substitutes by consumers (or that there is a realistic prospect of a chain of substitution). Historical evidence on the demand of bundles, or the relevant stand-alone components, could inform ComReg's view in this respect.
- Bundles included in the portfolio are such that the operators can switch to provide any of the bundles within the portfolio without incurring significant costs (e.g. the bundles would not rely on different wholesale inputs).

4.28 A portfolio approach would also allow economies of scale and scope from joint provision of products to be passed on to consumers. This is more appropriate where other firms can achieve their own scope economies by providing competing bundles. Competition among companies with different scope economies should be facilitated where possible as this will ultimately result in cost savings for consumers.

4.29 Therefore, the bundles portfolio would need to be set in a manner which ensures that consumers receive its full benefits and the mechanism cannot be abused by Eircom or lead to foreclosure of competitors. Therefore, careful design of the relevant portfolios is required to ensure that bundles that face similar demand and supply conditions are included in the same portfolio.

4.30 Furthermore, ComReg is of the view that a one portfolio approach would not be appropriate given the degrees of competition for certain bundles and given Eircom's advantage of incumbency across the wider customer base. Eircom still enjoys the benefits of incumbency over the wider national customer base where direct fixed line competition is less prevalent, for example in Areas 3-5 of Figure 4 in particular. While some consumers are more sensitive to price than others, some consumers remain with what they see as the reliable Eircom service provider regardless of cost. For many of these customers who have not switched and are not on bundles, the margins tend to be high and may not be reflective of the more competitive bundles that new entrants sell in the market. To use the margins of the entrenched customer base of Eircom may not lead to a fair reflection of the margins available to new entrants and what might be a profitable business case over the medium to long term. It is also the case that due to the enduring incumbency in large sections of the country where no direct competition exists at all Eircom enjoys significant economies of scale and scope not enjoyed by any other provider. Consequently, ComReg considers that options for setting portfolios of bundles include (it should be noted that a bundle must always include fixed retail narrowband access in order to be subject to the net revenue test under Decision D07/61):

1) Applying the test for two separate portfolios: (1) business and (2) residential bundles; *or*

2) Applying the test for two separate portfolios: (1) voice-only bundles and (2) voice and broadband bundles; *or*

3) Applying the test for two separate portfolios: (1) Bundles (including voice only bundles) sold in Larger Exchange Area (2) bundles sold in other areas; *or*

4) Combining 2) and 3) above to provide for three portfolios. (1) voice-only bundles (2) broadband bundles sold in Larger Exchange Area and (3) other broadband bundles; *or*

5) Applying the test separately for three separate portfolios of: (1) business bundles (2) residential broadband bundles based on NGB WBA inputs, (3) all other residential bundles / offers.

4.31 ComReg has analysed the current retail services and wholesale product set of Eircom and compared them to the wider market to get a better understanding of the comparative bundles on sale. ComReg is of the preliminary view that one of options 3 or 4 above may be the most appropriate as, subject to the Larger Exchange Area being set appropriately; it reflects the current viability of broadband provision by Eircom and OAOs. ComReg considers that either of these options strikes the right balance between allowing Eircom some pricing flexibility and ensuring that OAOs (who have fewer customers and a less differentiated customer base than Eircom) can remain competitive in the provision of bundled services

4.32 ComReg's initial analysis indicates that the treatment of voice only bundles separately as proposed in Option 4 may not have a material impact on the test and therefore, subject to respondents' views and other relevant evidence, proposes Option 3 for now as the simplest way forward. Furthermore, there is some protection for OAOs in that Eircom must also pass an individual bundle test based on a lower cost standard than ATC for retail calls — this is discussed further in the section relating to retail costs for retail calls. Therefore, the risk of Eircom selling a particular bundle significantly below cost as its costs are subsidised by the other higher margin bundles (e.g. business, voice only) within the portfolio is somewhat minimised by the individual bundle test. Importantly, there would also be an over-riding competitive assessment of proposed bundles to assess the possible anti-competitive effects of potential non-compliant bundles. ComReg recognises the importance of ensuring that only those bundles which would cause competitive and consumer harm are deemed non-compliant.

4.33 <u>ComReg would welcome views on the proposals to aggregate certain bundles for assessment in the net revenue test.</u>

Proposal: There will be two portfolios for assessing bundles under Part 1 of the net revenue test. The two portfolios are: Portfolio (1) comprising all Bundles (including voice only bundles) sold within the Larger Exchange Area; and Portfolio (2) comprising all Bundles sold outside the Larger Exchange Area.

STEP TWO: PROPOSALS IN RELATION TO THE COMPONENTS WITHIN THE NET REVENUE TEST

4.34 ComReg has set out below its proposals for the components of the net revenue test.

REVENUE:

<u>COMPONENT ONE:</u> Package Price and Calls Revenue

4.35 ComReg is of the preliminary view that it is appropriate to continue to use the average monthly revenue from an individual bundle as the revenue total in the net revenue test. That is, the test will consider both the package price of the bundle in effect in the market at the time and the revenue earned on average on components that are outside the bundle allowance e.g. calls in excess of free call allowance, broadband usage in excess of download allowance, usage above mobile add-on etc. ComReg's preliminary view in relation to promotional pricing is at paragraphs 4.102- 4.105.

Proposal: The calculation of revenue in the net revenue test to remain unchanged. This applies to both the individual bundle and portfolio assessment.

COSTS:

<u>COMPONENT TWO:</u> Wholesale input costs

4.36 This is discussed in Chapter 5.

<u>COMPONENT THREE:</u> Associated retail costs of narrowband and broadband wholesale inputs

4.37 Currently in the net revenue test, narrowband retail costs are based on the retail-minus 14% applicable to SB-WLR, while broadband retail costs reflect the retail-minus output of the D01 / 06 SEO margin (price) squeeze test. This approach ensures that the full monthly retail price of both narrowband and broadband line rental is considered in the net revenue test.

<u>Narrowband retail costs:</u>

4.38 In the case of narrowband retail costs, ComReg recognises that the retail-minus 14% currently in place for SB-WLR is based on the aggregate of PSTN and ISDN connections and rentals. Therefore, in the proposed revision of the retail fixed narrowband access price control due in 2012, the price control could consider PSTN rental separately to that of ISDN and connections. However, ComReg would note that the current price for SB-WLR is a maximum price and may be amended downwards by Eircom where appropriate, either on a promotional or a permanent basis subject to the required notification and approval process applicable to that market.

Proposal: Narrowband retail costs in the net revenue test will remain calculated by reference to the retail-minus price control for SB-WLR where the SB-WLR remains at the maximum price allowed i.e. 14% of retail price for retail line rental. This applies to the individual bundle and portfolio assessment.

Broadband retail costs:

4.39 In the case of broadband retail costs, these are discussed in Chapter 9 relating to WBA. The preliminary view is that it is appropriate to keep broadband retail costs based on a SEO pending the move to a cost-based price control for the setting of maximum prices for WBA which, subject to respondents' views and other relevant evidence to that separate consultation, could potentially be in place approximately one year from now. However, in the event that a cost-based WBA price control is not in place by that time, subject to respondents' views and other relevant evidence, ComReg may amend the D01/06 margin squeeze test from the current SEO basis to that of an EEO basis. This is discussed in more detail in Chapter 9.

Proposal: Broadband retail costs will for the time being remain calculated by reference to the SEO under D01/06. In 2012, D01/06 may potentially be amended to EEO or replaced by a cost-based price control, at which point the SEO test may no longer apply (subject to separate consultation) or may be replaced by an EEO test. This applies to the individual bundle and portfolio assessment.

COMPONENT FOUR: Wholesale and retail costs associated with retail calls

4.40 Currently, the net revenue test reflects all applicable wholesale input costs (e.g. MTRs and the ATC of retail costs. The costs are based on historic costs. There are possible revisions that could be made and these include using forward-looking costs for known changes to wholesale prices and using a lesser cost standard for retail costs for retail calls for the individual bundle assessment.

Costs: forward-looking view

4.41 In relation to other wholesale and retail input costs, such as interconnection costs, MTRs etc., currently the net revenue test uses the actual price / cost in effect at the time for such inputs. In relation to out-payment costs (e.g. international out-payments), the actual out-payment costs incurred by the SMP operator are used.

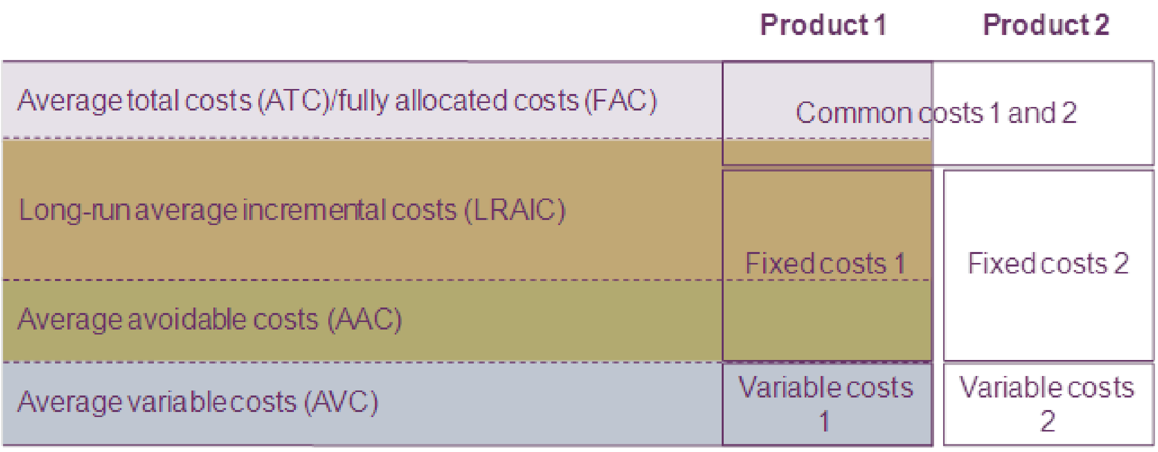
4.42 ComReg now proposes that where there is clear, unambiguous and robust evidence of future changes to input prices / costs over the average customer lifetime e.g. known MTR/Fixed Termination Rate ('FTR') reductions, the net revenue test should take account of these. ComReg considers that not to do so may put Eircom at a commercial disadvantage and delay end-users benefiting from reduced input costs now. The use of forward-looking costs would require retrospective monitoring to ensure that the cost reductions claimed did occur.

Preliminary view: Subject to robust and appropriate information, the net revenue test may be adjusted to reflect known future changes in wholesale and / or retail cost over the average customer lifetime. This will be monitored retrospectively. This applies to the individual bundle and portfolio assessment.

Appropriate measure of retail cost

4.43 The issue as to the appropriate measure of retail cost to be applied to retail calls was discussed extensively by ComReg in response to Consultation Document No. 09/43[24] and Consultation Document No. 10/01. In response to Consultation Document No. 10/01, all respondents except Eircom were of the view that ATC is appropriate while Eircom maintained that a cost measure other than ATC is appropriate.

4.44 The appropriate cost standard can be between the lower threshold of average variable cost (‘AVC’) toward the respectively higher thresholds of average avoidable cost (‘AAC’), then Long Run (Average) Incremental Cost (‘LRAIC’) and then ATC. This can be presented graphically as follows and is discussed further in the sections below:



Is AVC an appropriate measure of cost to be applied?

4.45 AVC approximates the variable cost of producing an additional unit of output. ComReg is of the preliminary view that AVC would not be an appropriate measure of cost to be applied as it is too low a cost threshold (for the reasons set out below). AVC does not consider fixed costs, which are the major cost components faced by telecom operators. Therefore, ComReg believes that applying a cost standard on this basis could significantly constrain the potential for entry by efficient entrants. ComReg believes that to use such a cost standard could lead to a medium to long term exit of operators who cannot sustain an entry strategy that may involve loss leaders for example.

4.46 ComReg welcomes views as to whether AVC should be used as the appropriate cost measure in the net revenue test.

[24] See ComReg document No. 09/53s ‘Extension of April 2009 Direction requiring Eircom to refrain from launching proposed 1MB and 3MB Family “free calls to meteor” TalkTime bundles - Submissions received from respondents dated 13 July 2009

Is AAC an appropriate measure of cost to be applied?

4.47 The precise definition of AAC depends critically on its actual implementation. For example, AAC may include avoidable fixed cost elements in addition to variable costs, depending on the timescale over which AAC is assessed. Therefore, these timescales would need to be clearly defined if AAC was to be considered in the net revenue test.

4.48 ComReg considers that AAC are the avoidable variable and incremental fixed costs of the additional sales of the product in question. The inclusion of fixed costs which would otherwise be avoided if the incremental output were no longer produced distinguishes AAC from AVC. Furthermore, the exclusion of a mark-up for overall fixed and common retail costs distinguish AAC from ATC. More specifically, AAC represents the avoidable costs of developing, launching, marketing and servicing each individual product element of the new bundled product. That is, each product/service which constitutes the new bundled product should be treated as a discrete element which is incremental to the retail fixed narrowband service provided by the SMP operator. This means that general fixed and overhead costs are excluded, though not the fixed development, launch and any other costs directly attributable to the bundled products and which would be avoided should they cease to be provided.

4.49 As the AAC standard does not include provision for (non-avoidable) fixed costs and common costs in a net revenue (ex-ante imputation) test, it could be argued that this provides the SMP operator with an advantage given the broad range of products and services over which it could conceivably recover such common costs. Entry/expansion by efficient OAOs, albeit with lower economies of scale and scope than Eircom, could thereby be impeded.

4.50 ComReg believes that ex-ante price controls should seek to ensure entry, and hence, the cost benchmarks that incorporate common costs should be warranted, as SMP operators are assumed to enjoy economies of scope that are not achievable for new entrants. Critically, ComReg believes that the decision to enter the market depends on the expectation that fixed and common costs are going to be recovered; not only additional avoidable costs incurred by the SMP operator. The reasoning behind this is that an entrant would enter a market only if it considered that it would be profitable to do so, taking into account all the costs that it would have to incur in order to enter the market and sustain a competitive position i.e., the fixed, common, joint and variable costs. Cost measures such as AAC do not ensure this as the total full costs of an operator are not covered. This view is supported by the ERG:

"…Avoidable costs are typically employed in ex post predatory pricing cases and here, they are defined as costs that the vertically integrated SMP firm could avoid if it decided to close its downstream operations while continuing to provide the upstream input to third parties. However, avoidable costs are also subject to criticism. In the context of an ex-ante regulatory tool, they may provide too low a threshold for retail prices, constraining the potential for entry by efficient entrants when the avoidable cost standard does not guarantee the recovery of the fixed costs of entry. Similarly, pricing at the avoidable cost level could even mean that competitors who provide a competitive constraint could be excluded. This is especially so if there are common or joint costs between different downstream services. Accordingly, the use of fully allocated costs as a proxy for average total

cost has also been put forward as an alternative cost measure or the allocation of common costs to the LRIC calculation." [25]

4.51 Therefore, ComReg is of the preliminary view that to apply an AAC cost rule in an ex-ante context could lead to sub-optimal entry conditions with little entry occurring. This would be to the detriment of competition and, in turn, consumers.

4.52 Therefore, given ComReg's statutory objective to promote competition, as well as taking account of the current state of market development of retail fixed narrowband access in Ireland, ComReg is of the preliminary view that the use of an AAC test in an ex-ante context to assess whether a bundle that includes retail fixed narrowband access is reasonable is not appropriate.

4.53 ComReg would appreciate any comments respondents may have on the use of AAC and whether it should be used in the net revenue test to assess whether a bundle is reasonable.

Is ATC or LRAIC the appropriate measure of cost to be applied?

4.54 The European Commission in its 'Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings'[26] noted that:

"*Long-run average incremental cost is the average of all the (variable and fixed) costs that a company incurs to produce a particular product. LRAIC and average total cost (ATC) are good proxies for each other, and are the same in the case of single product undertakings. If multi-product undertakings have economies of scope, LRAIC would be below ATC for each individual product, as true common costs are not taken into account in LRAIC. In the case of multiple products, any costs that could have been avoided by not producing a particular product or range are not considered to be common costs. In situations where common costs are significant, they may have to be taken into account when assessing the ability to foreclose equally efficient competitors.*"

4.55 Therefore, as noted by the European Commission above, ComReg does recognise that LRAIC and ATC are good proxies for each other in the case of single product provision. When applying the net revenue test to individual bundles and where the promotion of efficient entry is a key ex-ante regulatory objective, ComReg believes regulators may only have a choice between a LRAIC or an ATC approach, where regulators may opt for LRAIC (in countries where competition is more developed) or for ATC (in countries where competition is not mature or effective).

4.56 LRAIC generally provides a higher cost benchmark than AAC but, as inter service common costs are not taken into account, provides a lower cost reference than ATC where multiple services are at issue.

4.57 ATC is the cost standard currently used in the net revenue test and ComReg considers that the use of ATC remains appropriate in light of ComReg's statutory

[25] At para 60 & 61 of ERG 09(07) 'Report on the Discussion on the application of margin squeeze tests to bundles' dated March 2009

[26] C (2009) 864 dated 9 February 2009 – at footnote 18

objectives under Section 12 of the Communications Regulation Act 2002 to promote entry, competition and protect the interests of end-users.

4.58 In the context of an ex-ante regulatory tool to be applied by ComReg, ATC is the appropriate ex-ante cost basis to adopt as it enables a potential entrant to recover all its efficiently incurred costs. ATC requires an operator with SMP to price at levels that include appropriate amounts of variable, fixed and common costs, which is the calculus faced by any operator when deciding to enter or expand. For example, an operator will consider the current and future potential competitive environment (including price) when formulating its business plan when deciding to enter or expand in the market. ComReg is of the preliminary view that this is the most appropriate way to promote competition under regulation, and to avoid further deterioration in the already weak nature of competition in SMP markets.

4.59 Under the present market circumstances in Ireland, ComReg believes that it is legitimate and appropriate for ComReg to use ATC as the base for calculating Eircom's retail costs in an ex-ante context assessment of retail bundles that include retail fixed narrowband access at the portfolio level. Looked at differently, ComReg believes that relying only on any other cost measure would exclude any assessment of common costs and would therefore ignore the market entry or expansion realities faced by OAOs and new entrants.

4.60 ComReg considers that this position is supported by the continued investment in infrastructure by OAOs, Eircom and alternative platforms which ComReg welcomes. For example, Eircom[27] will spend €100 million upgrading its network; UPC[28] has committed a further €80 million investment to extend the reach of its network which will also create 50 new jobs; and BT Ireland/Vodafone have and continue to invest significant capital in their fixed broadband infrastructure. There are a number of smaller niche players who also play a key role in broadband development and innovation and employ in aggregate a significant number of people. Efficient players need to be considered, as well as the implications any price changes the SMP operator might make would have on their future in the market.

4.61 Therefore, ComReg remains of the view that ATC is the appropriate measure of cost to be applied and this should be be applied to the portfolio of bundles. However, ComReg is of the preliminary view that a lower cost standard, LRIC - estimated by ComReg in this instance from Eircom's accounts as ATC less common costs and fixed indirect costs - could be used for retail costs associated with retail calls in individual bundles within the portfolio and this is discussed in further detail below. The discussion below <u>*relates to retail calls only*</u> for now as the other retail costs are calculated by reference to their applicable retail-minus price control and different approaches in the net revenue test would require changes to their respective Decisions. However, ComReg intends to review the retail-minus price control for SB-WLR and WBA in a separate consultation process — which will consider the merit in revising its approach to reflect the proposal for retail calls as discussed below.

[27] Announced 28 July 2011 see: http://www.irishtimes.com/newspaper/breaking/2011/0728/breaking6.html

[28] Announced 29 July 2011 @ http://www.upc.ie/pdf/UPC%20creates%2050%20new%20jobs.pdf

ATC cost standard for aggregate / portfolio of bundles as approved by ComReg

4.62 ComReg proposes ATC will continue to be the applicable cost standard for retail calls but it is now proposed that this will apply for the aggregate / portfolio of bundles. For individual bundles, ComReg proposes that Eircom may sell below ATC on a case by case basis.

Proposal: ATC is the cost standard for the assessment of Eircom's bundles at the portfolio level to ensure they are and remain profitable.

<u>Source of cost data and reconciliation to audited accounts</u>

4.63 Currently, the ATC data for retail calls used in the net revenue test is sourced from Eircom based on cost allocations from the latest set of its separated accounts which are subject to an external audit. However, with a different net revenue test for the Larger Exchange Area, there may be merit in Eircom disaggregating its ATC data for retail calls, and later for retail broadband if EEO is used, between exchanges inside and outside the Larger Exchange Area when defined — <u>ComReg would welcome views on this</u>. Therefore, ComReg proposes that ATC is reconciled to regulatory accounting information from Eircom which is based on its audited separated accounts.

Proposal: ATC is based on and reconciled to Eircom's regulated accounting information based on its audited separated accounts. ComReg seeks views as to whether ATC should be / can be disaggregated between Larger Exchange Area and outside the Larger Exchange Area.

<u>LRIC for retail calls in individual bundles:</u>

4.64 In relation to the cost standard to be applied for retail calls in individual bundles within a portfolio, ComReg is now considering whether to allow a lower cost threshold subject to the proviso that the applicable portfolio of bundles passes ATC.

4.65 ComReg considers that this approach would be more consistent with that produced in competitive markets —where operators make decisions on single and marginal bundles based on the avoidable costs of that bundle / product. Since LRIC includes all costs related to the additional output it enables an analysis of incremental cost recovery and allows operators to make an informed business decision on that additional individual bundle. However, on a global level an operator would not be able to use this cost standard to inform its business decision as the incremental revenue attained from such bundles on aggregate basis may not make adequate contribution towards fixed and common costs. Consequently, ComReg is proposing a LRIC standard for the retail costs associated with retail calls which in this respect ComReg considers to be ATC less common costs and fixed indirect costs. ComReg believes this is an important allowance as to insist on passing an ATC for all bundles may be too restrictive on retail innovation and the ability to test demand etc.

4.66 As such, due to the proviso, if an individual bundle will account for most of the sales within an aggregate of the portfolio of the bundles, it must cover its ATC to ensure that the aggregate of the bundles passes ATC. In other words, if an individual bundle is a bundle sold to the majority of Eircom customers within the portfolio it must cover all (or most) of its retail calls' ATC to ensure that its aggregate portfolio of the bundles passes ATC. If Eircom does not cover these costs then it is likely to incur losses in the medium to long run which is not desirable for either Eircom or the telecommunications sector where a race to the bottom can lead to damaging consequences.

What are common costs?

4.67 ComReg regards common costs as costs incurred across the whole organisation regardless of product — so that the product does not directly benefit from the cost e.g. redundancy costs, asset impairment costs, general finance function costs, general corporate services costs, CEO salary, regulatory affairs costs, cost of voluntary leaving programmes.

What are fixed indirect costs?

4.68 ComReg regards fixed indirect costs as the indirect costs[29] that do not change with an increase or decrease in output e.g. depreciation, software licence costs (that do not vary per unit), building costs, pension provisions, exceptional items. Therefore, ComReg does not propose to include such costs in the cost standard for an individual bundle as such fixed indirect costs are akin to common costs.

Preliminary conclusion on cost standard for retail calls in individual bundle

4.69 Therefore, it is proposed that the retail calls cost standard for individual bundles will be LRIC which is estimated from Eircom's regulatory accounting information (which is extracted from Eircom's audited separated accounts) as ATC less common costs less fixed indirect costs subject to the overall proviso that the aggregate of bundles in the portfolio it is included in covers its ATC.

Proposal: LRIC (estimated in this instance from Eircom's regulatory accounting information as ATC less common costs and fixed indirect costs) to be the cost standard for retail costs for retail calls in the assessment of Eircom's bundles at the individual bundle level. Retail costs associated with broadband and retail line rental remain set by reference to their respective retail-minus price controls.

<u>COMPONENT FIVE:</u> Unregulated products and services that do not rely on retail fixed narrowband access

4.70 This section discusses the implications of the inclusion of unregulated products and services that do not rely on retail fixed narrowband access, such as mobile voice, mobile broadband, TV, Phone-watch alarm system, for the net revenue test. At the outset, ComReg wishes to make clear that it is not the intention to of ComReg to restrict Eircom to offer new bundles for the benefit of end users and to enter new markets. ComReg wishes to make clear that in relation to the bundling of

[29] ComReg regards indirect costs as a cost allocated to the particular product as the product directly benefits from the total cost. These costs are not specific (direct) to one product but to a set of products e.g. general Marketing & Sales spend.

unregulated products and services, ComReg will always have due regard to the competitive context of the proposed bundling and will be proportionate where it is clear that there will be no anti-competitive effect but that the proposal bundling is for the benefit of retail customers.

4.71 ComReg believes that the fact that additional products are not provided over retail fixed narrowband access is not in itself a sufficient condition to conclude that Eircom's bundles would not create competition problems. A potential concern is that Eircom could re-enforce its market power in the Retail Fixed Narrowband Access markets by offering unregulated products and services at relatively too low a price in a bundle that includes retail fixed narrowband access. Another concern is that Eircom could leverage its market power to competitive markets, and would be able to undermine the effectiveness of the obligation not to unreasonably bundle. More specifically, the risk is two-fold:

(1) Efficient providers of the additional products may be unable to compete with Eircom because they do not have access to the relevant upstream input, rendering additional products un-replicable.

(2) Consistent with the arguments presented above in relation to the portfolio approach, there are sound reasons why ex-ante regulation should not require efficient entrants to provide a precisely equal product offering with the incumbent.

4.72 Given the above, ComReg believes that it is important that ComReg assesses the relative importance of the additional unregulated products and services to the bundle, i.e. the extent of consumer demand for the bundled offering vis-a-vis the standalone components, and the extent to which these bundles could be replicated by entrants / OAOs.

4.73 While there is a growing trend of mobile operators providing fixed line services there are also fixed line operators supplying mobile. Eircom's supply of bundled services incorporating both fixed and mobile components could potentially be pro-competitive and provide it with a mechanism for addressing network effects enjoyed by more established mobile incumbents for calls. ComReg thus considers that careful consideration is required in setting the required cost standard for unregulated products and services bundled with regulated products. However, if Eircom was able to price the incremental mobile voice below its LRIC for a sustained period of time by cross subsidisation from its retail narrowband access business, and assuming a significant level of demand for this bundled offering relative to the standalone components, this might raise the costs of entry/expansion to fixed and mobile markets for OAOs and further deter/delay competition in the Retail Fixed Narrowband Access markets.

4.74 At the same time, for the provision of certain unregulated products and services, ComReg recognises that Eircom could be regarded as the "entrant" and certain other operators could be regarded as the "incumbents". For example, in the provision of mobile voice, Eircom could be regarded as the "entrant" when compared to the scale of Vodafone and Telefonica (O2) in the provision of mobile voice. Similarly, in the provision of TV, Eircom will be an entrant and will not have the same scale as existing providers, UPC and Sky. Therefore, in these instances those "incumbent" operators in the provision of those services could potentially replicate Eircom's provision of certain unregulated services at the same or much lower level of unit costs. However, as UPC currently does not provide mobile voice and as Sky currently does not offer fixed and / or mobile voice — ComReg recognises that Eircom would currently be the only operator capable of providing fixed voice, mobile voice and TV together.

4.75 Therefore, for the bundling of other unregulated products and services that do not rely on retail fixed narrowband access, ComReg proposes that:

4.75.1 There should not be any cross-subsidisation between retail fixed narrowband access and the unregulated product. This mitigates the risk of any leverage.

4.75.2 The incremental revenues over the average customer lifetime (which can be different for different unregulated products and services) of the unregulated product in the bundle must cover its own long-run incremental costs ("LRIC"). If the incremental price of an additional unregulated product was lower than its (long-run) incremental cost, two principal effects could emerge:

(i) competition may be distorted in the markets of stand-alone (unregulated) products — a situation analogous to predatory pricing; and

(ii) entrants may be foreclosed from selling bundles effectively because they may not have access to the same suite of fixed and mobile wholesale products and where only short run incremental costs are recovered it is unlikely any OAO would have the incentive to enter these markets.

4.75.3 However, on a case-by-case basis where the bundling of the unregulated product does not account for a sufficient portion of the market and will not have a significant impact on competition, ComReg will consider allowing that unregulated product only cover its own AAC instead of its LRIC.

4.75.4 In the specific case of unregulated mobile services, the total Long Run Average Incremental Cost ("LRAIC+") of the relevant unregulated product should be recovered in the aggregate by all of that applicable unregulated service e.g. the aggregate of all mobile voice services (mobile voice/broadband offers by Meteor and E-Mobile whether in a bundle or outside a bundle) must cover at least the LRAIC+. As noted earlier, the European Commission in its 'Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings'[30] noted that: "*Long-run average incremental cost is the average of all the (variable and fixed) costs that a company incurs to produce a particular product. LRAIC and average total cost (ATC) are good proxies for each other, and are the same in the case of single product undertakings. If multi-product undertakings have economies of scope, LRAIC would be below ATC for each individual product, as true common costs are not taken into account in LRAIC. In the case of multiple products, any costs that could have been avoided by not producing a particular product or range are not considered to be common costs. In situations where common costs are significant, they may have to be taken into account when assessing the ability to foreclose equally efficient competitors.*"

4.76 ComReg does not believe it is practical for ComReg to continue to apply the standalone retail price for unregulated products and services in the net revenue test.

[30] C (2009) 864 dated 9 February 2009 – at footnote 18

The standalone price may continue to form part of the assessment; however, it is unlikely that consumers will see the addition of products at standalone prices to be attractive. Evidence in the market place suggests that it is common to offer discounts when sold in bundled offers.

4.77 Consequently, based on the above, for the example of mobile voice, it is probable that Eircom would be able to bundle cheaper Meteor / E-Mobile offers for its retail fixed narrowband customers once the mobile voice covers its own LRIC and mobile voice as a whole covers its LRAIC+. Again, to be clear, no cross subsidisation between retail fixed narrowband access would be allowed. The Competition Authority[31] also acknowledged the threat of cross-subsidisation at the time Eircom purchased Meteor and set out conditions which are still in place.

4.78 As a result of the above, ComReg could allow, say, IPTV to only covers its AAC, which mainly relates to content, as it is a service in its infancy and one in which Eircom does not have any dominance as it is the "new entrant". Again, to be clear, no cross subsidisation between retail fixed narrowband access would be allowed.

4.79 To conclude and for the avoidance of doubt, in all cases, the onus would be on Eircom to ensure that it is compliant with the required cost standard based on information available to it. Currently, ComReg does not have any cost models for these unregulated products and services. However, ComReg would be able to request Additional Financial Statements ("AFS") where required to cover unregulated products and services and currently receives separated accounts for Meteor and E-Mobile respectively.

Proposal: Unregulated products and services when bundled with Retail Fixed Narrowband Access must pass their own LRIC. On a case-by-case basis and subject to no medium to long term competitive harm, AAC might be used instead of LRIC. In addition for unregulated retail mobile services, aggregate total revenues must exceed their LRAIC+ (including common cost) each year. These proposals apply to both the individual bundle and portfolio assessment.

COMPONENT SIX: Mailbox

4.80 Where the bundle packages include free mailbox, the wholesale monthly price of the mailbox as per the regulated retail minus price control as published in Eircom's Reference Interconnect Offer Price List must be taken to ensure an operator can replicate the offer. However, consideration would be taken of the applicable average take up of the mailbox and the wholesale price would be adjusted to reflect this. The retail costs as derived from the retail minus price control would also be considered here.

Proposal: No change proposed to treatment of mailbox costs (where included). This applies to both the individual bundle and portfolio assessment.

[31] http://www.tca.ie/images/uploaded/documents/2005-11-18%20News%20Release%20(Eircom-Meteor).pdf

STEP THREE: CASE-BY-CASE ASSESSMENT OF A BUNDLE'S REASONABLENESS

4.81 If a bundle fails the net revenue test, ComReg as a proportionate measure currently considers any robust evidence of retail efficiencies or increased customer lifetimes as a result of bundling in order to determine whether the bundle complies with the obligation under Decision D07/61 not to unreasonably bundle services. ComReg also considers the impact on competition and the ability of entrants to enter/remain in the market and promote sustainable competition in the medium to long term.

4.82 Therefore, currently, if a bundle fails the net revenue test and is selling retail fixed narrowband access below cost it does not automatically lead to that bundle being considered unreasonable — ComReg assesses other factors, which include inter-alia:

Retail efficiencies

4.83 For the purposes of applying the net revenue test, ComReg accepts that, in principle, it is appropriate to have regard to retail efficiencies and related savings, subject to the existence and / or quantum of such being demonstrated to ComReg's satisfaction. For example, such retail efficiencies could relate to cost savings derived from reduced billing and customer service costs to the extent that such savings could also be replicated by other operators. Therefore, full consideration will be given by ComReg to any efficiency gain presented which is substantiated with a sound rationale and robust supporting evidence.

4.84 ComReg does recognise that with the use of the retail-minus price controls to calculate the retail costs for broadband and line rental there may only be limited potential to recognise retail efficiencies. However, ComReg does recognise that there may be costs in effect "double counted" in both retail-minus price controls which are set for a stand-alone efficient operator; for example, a retail efficiency could be the double count of the costs associated with issuing the bill in the standalone retail cost stacks for broadband and line rental when those services are bundled together.

4.85 However, ComReg must assess any such claims of efficiencies carefully when the test is based on actual retail costs incurred from a previous period as many factors may have changed since that period. For example, the relevant volumes of the SMP operator may have reduced which may have increased the per-unit retail costs rather than reduced them due to efficiencies. Consequently, ComReg believes that it is highly important to understand in detail the underlying unit costs — as any bundle allowed due to perceived retail efficiencies could cause significant harm to the market where it is found ex-post that the bundle was in fact non-compliant — as the claimed retail efficiencies due to bundling were not real.

Proposal: ComReg proposes no change from current net revenue test. Retail efficiencies once supported by robust evidence can be considered in determining whether a bundle, which fails the net revenue test, is nonetheless compliant with the obligation not to unreasonably bundle services.

Increased customer lifetimes

4.86 Under the current net revenue test, any claim for increased customer lifetimes for bundles must be demonstrated to ComReg's satisfaction by robust supporting evidence.

4.87 An issue in the assessment of increased customer lifetimes is that bundled products are relatively new and that customers who avail of bundled products from the SMP operator are subject to a minimum twelve month contract. Therefore, there may not be a sufficiently long or robust set of data to inform a claimed longer customer lifetime for customers within bundles. Furthermore, any claimed increased customer lifetime is for existing customers on an existing bundled package and may not reflect the customer lifetime of a customer availing of a new bundled offer. Also, it is likely, given its position of incumbency, that the majority of customers availing of the SMP operator's bundles will be existing customers of the SMP operator and therefore it is unlikely that these customers have moved between operators.

4.88 OAOs may not have average customer lifetimes within bundles as long as those of Eircom and therefore this may need to be considered. Furthermore, OAOs, for the most part, have a base of customers that have left Eircom and therefore are customers who have moved between operators and may be more likely to do so again. Similarly, the average customer lifetimes within bundles in the Larger Exchange Area may be different.

4.89 Therefore, ComReg would appreciate respondents' views on this. ComReg would also welcome any data respondents may have on their average customer lifetimes for both their bundle and standalone customers respectively which can be submitted in confidence for ComReg's consideration.

Proposal: ComReg proposes no change from current net revenue test. Increased customer lifetimes once supported by robust evidence can be considered in in determining whether a bundle, which fails the net revenue test, is nonetheless compliant with the obligation not to unreasonably bundle services.

Competitive assessment

4.90 Currently, ComReg considers all available information to hand to consider the impact of the below cost selling of retail fixed narrowband access in a bundle on competing operators and the ability of entrants to enter/remain in the market(s) and promote sustainable competition in the medium to long term.

4.91 For example, relevant considerations which ComReg may take into account when assessing each bundle in its relevant competitive context include:

- Relevant commercial or strategic reasons for the bundled offer;
- The duration and scope of the bundled offer, as well as relevant product complementarities;

- Nature/composition of retail demand[32];
- Any asymmetry in product lines of market participants and ability of OAOs to replicate the bundled offer;
- Whether the pricing of the bundle in question is likely to have an appreciable effect on existing competitors or new or potential entrants to the affected market(s);
- Medium-to-longer term implications for retail pricing, innovation and consumers[33];

4.92 In line with ComReg's Strategy Statement and objectives set out earlier, it is the intention that all efficient OAOs, not only Eircom, have the correct incentives to enter/expand in the market for voice, broadband and other related services. Where there is no clear regulatory framework in relation to the relative pricing of regulated services and on what ComReg considers to be an appropriate margin squeeze test between Retail Fixed Narrowband Access bundles and competitive offers, this leads to uncertainty. The decision to build or buy wholesale services in order to compete in fixed retail markets may be undermined by short term pricing decisions of the incumbent which may be anti-competitive. For example, the bundling of mobile services with retail narrowband services at prices so low that other fixed and mobile players cannot compete against such bundled offers in the long term may lead to decisions to exit. No OAO may be in a position to remain in the market where short run incremental costs are all that is recovered and where the expectation is that prices will remain at these low levels. An SMP operator may, however, be in a position to sustain heavy losses in the mobile sector where it can leverage from high profits in SMP markets until such time as smaller operators have exited.

4.93 However, ComReg is also conscious of the fact that Eircom may sometimes need to sell unregulated services at a short run incremental cost basis to assess whether it wishes to enter/remain in a market in which it has traditionally not been present. Therefore, ComReg considers that a practical and proportionate regulatory approach is required on a case by case basis.

4.94 <u>ComReg would welcome respondents' views on the information that ComReg could utilise in its assessment of the impact of a below cost bundle on competing operators and entrants — and therefore determine whether it amounts to unreasonable bundling.</u>

Proposal: ComReg proposes no change from current net revenue test. A competitive assessment is undertaken before a bundle is found to be in breach of the obligation not to unreasonably bundle services.

[32] For example, if the market is broader than the bundled offer a relevant consideration will be what proportion of the overall market demand the bundled offer accounts for/is likely to account for and whether this proportion of the market is important to certain OAOs/entrants.

[33] For example, if the effect of the bundle is to impede entry/expansion by efficient rivals, then any short term discounting by the SMP operator would need to be assessed against the possibility of higher prices and a dampening of product innovation over the medium to longer term.

Other possible options for revisions to the net revenue test

4.95 ComReg has considered a number of potential scenarios which may impact whether the net revenue test needs to be revised. Each of these scenarios / circumstances is discussed in turn below including ComReg's preliminary views on each:

<u>When the bundle is a response to a competitor's bundle</u>

4.96 In relation to this proposal of a different net revenue test to assess the reasonableness of a bundle when it is claimed to be a direct response to competition, ComReg's preliminary view remains as noted in ComReg Decision D02/09 and Consultation Document No. 10/01, namely the test does not change when a bundle is claimed to be a response to a competitor's bundle.

4.97 ComReg believes that if entrants knew that the incumbent could respond to entry by dropping prices below efficient cost, this would increase the risk that the entrant would not be able to recover its fixed costs, and might therefore preclude efficient entry. The net revenue test has a clear underlying logic: if Eircom's pricing does not cover its ATC it is reasonable to assume, subject to the outcome of the complementary competitive assessment, that an efficient rival would also not be covering its full costs since Eircom has economies of scale and scope within the fixed sector that others are unlikely to be able to match. Other operators' ability to compete with Eircom would therefore be constrained, their incentives to enter would be weakened, and their ability to establish themselves as sustainable retail competitors in the longer term could also be hampered. ComReg welcomes respondents' views as to whether the test should be a different standard when a bundle offered by the SMP operator is claimed to be a response to a competitor's bundle.

Proposal: ComReg proposes no change to the current net revenue test. The net revenue test does not change when a bundle is claimed to be a response to a competitor's bundle. However, as is currently the case, the complementary competitive assessment will investigate the competitive context of the bundle.

<u>A different test for when a bundle is found unreasonable post launch?</u>

4.98 In relation to a bundle, for example, that has passed the net revenue test for, say, a year but, say, due to declining out of bundle revenue no longer passes the net revenue test – should a different test apply?

4.99 ComReg is of the preliminary view that a different test should not apply. As noted earlier, it is proposed that a competitive assessment should be conducted and if it is believed no competitive harm will come from allowing Eircom to continue to offer the bundle, e.g. if consumer demand for the bundled offer is particularly weak relative to the standalone components, ComReg would likely not find the bundle to be unreasonable even though it is below cost.

Proposal: ComReg proposes no change to the current net revenue test. There is no different test for bundles after launch.

Should Eircom be allowed "bank" / carry forward past margins?

4.100 In relation to a bundle, for example, that has a margin of €5 a month for the past twelve months, should Eircom be allowed use this bank of €60 margin (€5 * 12 months) to offer a discount of, say, €10 over the next six months for customers on that bundle?

4.101 ComReg is of the preliminary view that margins cannot be "banked" / carried forward. To allow Eircom to do so could distort competition in the market.When there is no competition, Eircom could build a defensive bank of available margins for a bundle which Eircom would then use when a competing operator tries to make a competing offer to that bundle. ComReg proposes that the assessment of bundles should be on a case by case basis and consider the likely future impact; taking into account past performance and profitability may not be a useful indicator of likely anti-competitive effects.

Proposal: ComReg proposes no change to the current net revenue test. Past margins cannot be banked / carried forward.

Promotions and promotional discounts

4.102 While the duration of a promotion may play some role in its potential to foreclose a market, ComReg is of the preliminary view that the obligation not to unreasonably bundle services and all its facets still apply even if a bundle is only planned to be offered for a limited promotional period. ComReg believes that it would not make sense for promotions not to be subject to full regulatory controls. ComReg believes just because a bundle is offered for a promotional period only does not automatically demonstrate that there is no potential harm to efficient competitors[34]. Therefore, ComReg believes that a bundle must be reasonable at all times.

4.103 In relation to promotional discounts, for example, €10 off the headline price of a bundle for the first six months, ComReg currently regards a promotional discount to be reasonable if the cost of the promotional discount is covered over the average customer lifetime, which ComReg currently estimates to be 42 months based on the modelling of the SEO in the current Decision D01/06 WBA price control. However, ComReg exercises caution in the use of average customer lifetimes where it believes the 42 month assumption of D01/06 may not be appropriate for the particular circumstance of the bundle under review.

Proposal: No changed position - a bundle must be reasonable at all times and a promotional discount is considered reasonable if the cost of the promotional discount is covered over the average customer lifetime.

[34] For example, the 2009 legal proceedings concerned bundles that were available for sale within a six month promotional window but customers who availed of the promotion could avail of the bundle for the entire period of their customer lifetime with the SMP operator – therefore the impact on competitors and entrants was longer than the period of the promotion itself

Discretionary promotions / opt-ins

4.104 In relation to a bundle that has a discretionary / opt-in offer, for example, that allows new customers onto a bundle an additional discount, should the net revenue test apply the cost of this opt-in as if all customers on the bundle availed of it or should the net revenue test only recognise the cost of the opt-in offer for the new customers? An example of this would be a promotional discount for new customers on a bundle – therefore, these new customers with a promotional discount would only account for, say, 10% of the bundle customer base. The question is whether the actual cost of the promotion for the 10% of the customers is taken or is it assumed that the cost of the promotion applies for 100% of the customers on the bundle.

4.105 Assuming 100% take-up / opt-in means Eircom cannot take advantage of its incumbency / large installed base to fund new customer offers, since OAOs do not have the same large installed customer base. ComReg is of the preliminary view that the net revenue test is not changed and 100% opt-in should continue to be used as this reflects the cost that competing OAOs would face to offer a replicable bundle to their new customers or to keep their existing customers.

Proposal: ComReg proposes no change to the current net revenue test. Discretionary promotions / opt-ins are assumed to have 100% take-up.

Q. 1. Do you agree or disagree with the proposals / preliminary views expressed by ComReg in relation to possible revisions to the net revenue test? Do you have any views on the matters ComReg seeks further input on in the above? Please give a detailed response with supporting data where appropriate to support your view.

5 Appropriate wholesale input cost for use in the net revenue test

5.1 Setting a revised wholesale input cost for use in the net revenue test is an important consideration of this consultation as subject to respondents' views and other relevant evidence, it could offer Eircom the greatest flexibility to offer cheaper bundles to end users in certain areas. Therefore, this issue is dealt with separately in this Chapter.

5.2 In order to offer line rental and broadband, an operator could potentially utilise the following wholesale inputs:

- SB-WLR and WBA (Bitstream);
- SB-WLR and LLU Line Share;
- LLU (ULMP).

5.3 The net revenue test could utilise these different combinations of wholesale inputs, or a weighted average combination of all three, in its test to assess whether a bundle that includes retail fixed narrowband access is below cost. In deciding which wholesale inputs should be used for certain bundles in certain areas, ComReg's goal is to ensure that Eircom's bundles can be replicated by OAOs using Eircom's wholesale inputs.

5.4 Currently, the net revenue test uses SB-WLR and WBA (Bitstream) as the wholesale inputs in the net revenue test. These are the predominant wholesale inputs used as evidenced from the latest Quarterly Report[35] — which shows that OAO share of retail fixed narrowband access lines is around a third with the majority of this being use of SB-WLR. OAO share of DSL access is also around a third with the majority of this being use of Eircom's WBA.

5.5 It could be argued that the use of these wholesale inputs based on limited infrastructure investment in the net revenue test may advantage LLU operators to compete as Eircom must cover the higher price of the 're-sale' wholesale inputs of SB-WLR and WBA combined. However, countering this possible argument is the fact that an operator availing of LLU must also cover the high cost of up-front infrastructure investment required to avail of LLU and that LLU is currently only likely to be used in certain exchanges. In assessing what could be the appropriate wholesale input costs in a revised net revenue test, ComReg will consider the Areas set out in Figure 4 as follows:

<u>Area 1:</u>

5.6 In the current net revenue test applicable to Retail Fixed Narrowband Access, Eircom must use the wholesale inputs of SB-WLR and WBA for its retail narrowband and broadband offers in Areas 1 to 4. As Area 1 also largely reflects the footprint of the cable operator, UPC, and it is an area where unbundling is considered viable, Eircom and its wholesale customers may potentially face more competitive pressure in Area 1 over time.

[35] ComReg Document No. 11/66 'Quarterly Key Data Report: Data as of Q2 2011' dated 14 September 2011

5.7 ComReg believes there are a number of options open to Eircom in this regard. One option would be for Eircom to have a lower ULMP price reflective of the underlying costs in Area 1 only – the maximum LLU price was set on the basis of Area 1 and 2 together. However, Eircom could claim that a lower ULMP price would not benefit it as it would still be regarded as a SB-WLR+WBA customer in the net revenue test for Area 1 and this might create a competitive disadvantage for its retail arm. Therefore, using a different wholesale input cost in the net revenue test for Area 1 needs to be considered in this consultation.

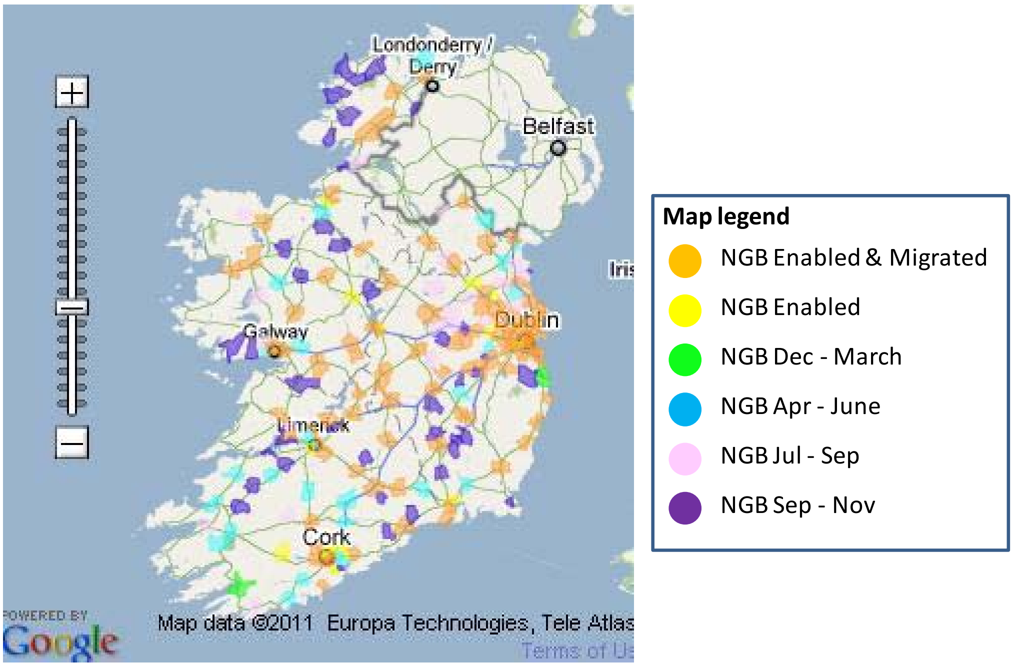
Area 2:

5.8 In setting the maximum ULMP price in Decision D01/10, ComReg considered this area as being likely to be unbundled. However, LLU take-up in Area 2 has been lower than assumed in the LLU pricing decision made in early 2010. ComReg considers it may be appropriate to consider a different wholesale input cost for Eircom in its net revenue test for this area which may encourage LLU take-up in this area.

Area 3:

5.9 In relation to Area 3, this reflects the footprint of Eircom's NGB area.

Figure 7: Current and proposed footprint of NGB / BMB (Eircom map @ [http://www.nextgenerationbroadband.ie/http://www.nextgenerationbroadband.ie/](http://www.nextgenerationbroadband.ie/))



5.10 As can be seen from the above illustrative map, which is amended from time to time by Eircom as networks are upgraded, the NGB footprint is concentrated on urban areas. It also covers a larger area than cable and LLU availability — however, Eircom notes that the areas currently covered by cable and LLU account for the majority of customers within the NGB area.

5.11 However, this area is in a footprint greater than the footprint assumed in the LLU price control model in Decision D01/10 (i.e. the LLU price control model only considers Area 1 and Area 2). Therefore, ComReg considers that use of the current ULMP maximum price of €12.41 which reflects mainly Area 1 and 2 BU- LRAIC costs, would not be appropriate in Area 3 as Area 3 represents a higher unit cost for LLU based on the BU-LRAIC. Furthermore, LLU may not be viable in the short-medium term in this area and ComReg considers SB-WLR and WBA are likely to be the predominant wholesale inputs used by OAOs. However, as stated earlier, this Area is also likely to correspond fairly closely to Eircom's ultimate footprint for NGA services. If NGA roll out does take place and if Eircom were to offer an acceptable unbundling product at wholesale level that was viable across this footprint, ComReg considers that this Area could be categorised in a similar manner to Areas 1 and 2 if not now, then as soon as industry and ComReg had more clarity in respect of NGA roll out.

Areas 4 & 5:

5.12 ComReg believes that it would be inappropriate to allow Eircom to use an equivalent LLU+ as its wholesale input in Area 4 or Area 5 where it is based on BU-LRAIC costing methodology. ComReg considers that for these areas it would likely remain appropriate for the net revenue test under D07/61 to be based on the wholesale input costs of SB-WLR and WBA as these are the wholesale inputs on which any competition in these areas is predominantly based at this stage and is likely to be over the next few years. In fact in some of these geographic areas (called "Area 5" in Figure 4) fixed DSL broadband is not and may not be available from Eircom due to the cost of providing a service and may only have National Broadband Scheme / Rural Broadband Scheme provision in that area. ComReg considers that upgrades to broadband related infrastructure by commercial operators is likely to remain in the more densely populated areas. However, liberalised spectrum may facilitate wireless broadband provision in these areas to ensure broadband is rolled out in less densely populated areas where commercially feasible.

Larger Exchange Area:

5.13 Having considered the above, ComReg considers that it would only be appropriate to consider a revised wholesale input cost in either Areas 1 – 2 of Figure 4 or Areas 1 – 3 of Figure 4. Subject to respondents' views and other relevant evidence, these areas would be defined as the 'Larger Exchange Area' and in this Larger Exchange Area ComReg proposes that Eircom should be able to use a different wholesale input cost.

5.14 Consequently, in the below, ComReg discusses the proposed use in the net revenue test of a new weighted average cost of wholesale inputs in the Larger Exchange Area. ComReg also seeks view as to when / where Eircom could use LLU+ as the applicable wholesale input in the Larger Exchange Area as LLU take-up and competition develops.

Proposal: ComReg will define an appropriate area ("Larger Exchange Area") corresponding to those areas where uptake of unbundled services, whether LLU and/or virtual unbundling in NGA, is likely to be viable. Subject to respondents' views and other relevant evidence, the Larger Exchange Area could be either Areas 1-2 of Figure 4 <u>OR</u> Areas 1-3 of Figure 4.

<u>Use of weighted average mechanism that recognises actual use by OAOs of different wholesale inputs in the Larger Exchange Area</u>

5.15 It is proposed that for areas outside the Larger Exchange Area the use of SB-WLR and WBA (Bitstream) as the applicable wholesale inputs in the net revenue test would continue.

5.16 However, for the Larger Exchange Area, a mechanism that reflects the actual use of different wholesale inputs is proposed. Therefore, ComReg proposes a weighted average of the different wholesale inputs used by OAOs in the Larger Exchange Area as the applicable wholesale input to use in the net revenue test in that area.

5.17 The proposed weighted average of all the applicable wholesale inputs used by OAOs in the Larger Exchange Area would work as follows. The three applicable wholesale inputs and all associated costs would be taken based on the prices in effect and current cost models. **The examples and unit costs below are indicative only based on assumptions made. Supporting cost models have not been finalised. ComReg will use the most up to date information available at the time of any review of a bundle proposed. The costs below therefore may be higher or lower depending on such a review and should only be used as guidance.**

5.18 The first applicable wholesale input is SB-WLR and WBA. This would be based on the SB-WLR price plus the weighted average price of all the wholesale equivalent of NGB, BMB. As BMB is priced based on usage, an assumption has to be made in relation to the Mbps usage that sets the wholesale price and ComReg proposes that this will be set by reference to the finalised minimum price floor model for WBA. For this example, ComReg proposes to use an average usage of 75kbps for the 8Mb BMB product and 150 kbps for the 24Mb BMB product as the assumed usage facing an equivalent operator.

5.19 Consequently, assuming a hypothetical example of 80% customers on 8Mb BMB and 20% on 24Mb BMB, and using Eircom's current wholesale pricing for its BMB products and making an assumption of 75 kbps for 8 Mb BMB and 150 kbps for 24Mb BMB , this would result in a possible monthly wholesale input price of:

100% SB-WLR	€18.02
80% 8Mb BMB (€4.90+.05*75kbps = €8.65)	€6.92
20% 24Mb BMB (€7.65+.05*150kbps=€15.15)	€3.03
Bitstream Ethernet Connection Service Backhaul (Est.)	€0.50
Total possible SB-WLR and BMB wholesale input	**€28.47**

The assumptions above are hypothetical and can be amended to show likely impacts.

5.20 The second applicable wholesale input is SB-WLR and Line Share plus all the relevant costs facing a REO ("LS+"). Again, ComReg proposes to use assumptions and costs consistent with those made in the minimum price floor model for WBA[36] when it is finalised. Consequently, (subject to the outcome of the consultation process provided for in Consultation Document No. 10/108) the DSLAM and Transport costs will be informed by the minimum price floor model for WBA when it is finalised which includes the following costs facing a LLU Line Share operator of:

- Capital and installation cost of ISAMs plus return on capital
- Accommodation and power costs for ISAMs
- Costs for aggregation nodes and BRAS
- Direct operating costs
- Access network costs
- Backhaul costs
- Repair costs for broadband line
- Connection and provisioning costs

Therefore, as an example, ComReg considers all the relevant monthly costs for this applicable wholesale input could be as follows:

[36] See Consultation Document No. 10/108 dated 22 December 2010

SB-WLR – per Eircom RIO	€18.02
Line Share – per Eircom ARO	€0.77
DSLAM costs – 2011: €7.65 - €0.77[37] (as per current DRAFT of WBA minimum price floor model - subject to finalisation)	€6.88
Transport cost – 2011: €50Mbps * 75kbps (assumed usage) (as per current DRAFT of WBA minimum price floor model-subject to finalisation)	€3.75
Connection and disconnection charges (included in DSLAM)	€0.00
Total possible SB-WLR and LS+ wholesale input	**€29.42**

5.21 The third possible applicable wholesale input is LLU+. This would use the ULMP price / network input cost in effect in the relevant area as appropriate. It would use the same DSLAM and Transport costs as modelled by ComReg, which are based on the minimum price floor model for WBA which is under consultation, and it would also add a monthly cost for Fault Repair to reflect the likely average cost faced by an LLU operator. Therefore, for this example, ComReg considers all the relevant monthly costs for this applicable wholesale input could be as follows:

Possible LLU+ wholesale input floor in Larger Exchange Area (if Area 1 and 2):

ULMP [149 exchanges] – if only Area 1 and 2	€12.41
ULMP Fault Repair [149 exchanges] (€117.31*8%) / 12 [Fault repair actual cost * fault % used in ULMP price control model]	€0.81
Line card (included in DSLAM cost below)	€0.00
ULMP connection and disconnection charges	€0.90
Plus WBA minimum price floor if broadband is offered:	
DSLAM costs (as per current DRAFT of WBA minimum price floor model - subject to finalisation)	€6.88
Transport costs (as per current DRAFT of WBA minimum price floor model - subject to finalisation)	€3.75
Possible total LLU+ wholesale input in Area 1 and 2	**€24.75**

5.22 A further complexity is to question if the current price of LLU is the correct starting point for this calculation since, depending on how the Larger Exchange Area is

[37] Based on draft result at page 10 of Consultation Document No. 10/108 – approach and results subject to review of responses to that consultation and notification to European Commission. When finalising model, ComReg will also consider any new appropriate backhaul product from Eircom that may be available by then for use by OAOs.

defined, this price may represent the costs of only a subset of the Larger Exchange Area i.e. only Areas 1 and 2. If Area 3 is included then the starting point will be higher than €12.41.

5.23 To get the applicable weighted average of all the applicable wholesale inputs the % usage of each applicable wholesale input by OAOs in the Larger Exchange Area will be used – it is proposed that this would be updated quarterly based on actual usage. Therefore, assuming for this hypothetical example that OAOs use 60% SB-WLR and BMB, 30% SB-WLR and Line Share and 10% LLU in Area 2 only of the Larger Exchange Area would result in a weighted average wholesale input as follows:

Example of possible Weighted Average wholesale input cost for Larger Exchange Area:

(60% * €28.47) + (30% * €29.42) + (10% * €24.75)	€28.39

5.24 As can be seen, for the example above, the weighted average wholesale input proposed for use in the Larger Exchange Area is similar to that for the full SB-WLR and WBA input currently in use. This is mainly due to the low level take-up of LLU by OAOs in the example. Therefore, as the actual use of LLU by OAOs increases, the weighted average wholesale input cost would decrease for Eircom which would act as an incentive for Eircom to encourage OAOs to use LLU.

5.25 Subject to respondents' views and other relevant evidence, ComReg proposes such an approach as set out above to be conducted quarterly based on latest available data as per ComReg's Quarterly Reports and relevant data from Eircom provided under s.13D(1) of the Communications Regulation Act 2002, as amended. Therefore, if the Direction following this consultation was in effect on 31 March 2012, it is proposed that the weighted average wholesale input would be used by Eircom in the Larger Exchange Area from 1 April 2012 based on the usage of wholesale inputs by OAOs in the Larger Exchange Area in the quarter 1 January 2012 – 31 March 2012. It is proposed that the weighted average input cost for use by Eircom in Larger Exchange Area would be revised on 1 July 2012 based on actual usage by OAOs in the quarter 1 April 2012 – 30 June 2012. It is proposed that this quarterly adjustment of the weighted average input cost would continue until Eircom is potentially allowed following further consultation to use an alternative appropriate network input to replace the weighted average as the applicable wholesale input cost in the Larger Exchange Area.

5.26 Respondents should be aware that revising the net revenue test input to reflect the cost of the Larger Exchange Area would allow Eircom the flexibility to price bundles more cheaply where it chose to do so. For example, defining the Larger Exchange Area based on Areas 1 and 2 of Figure 4 would likely allow Eircom greater flexibility as the weighting of LLU use by OAOs in those areas are higher. If the Larger Exchange Area was defined to include Area 3 of Figure 4, the flexibility would likely be lower as the weighting of LLU use by OAOs would be lower when considered over the higher OAO customer base of these areas and, furthermore, there is likely to be a higher LLU network input cost associated with Area 3.

Proposal: For bundles sold within the Larger Exchange Area, the net revenue test will reflect the weighted average cost of Eircom's wholesale inputs sold to OAOs based on actual usage by OAOs of each applicable wholesale input in the Larger Exchange Area at the end of the previous quarter. This weighted average wholesale network input cost would remain in place until (subject to further consultation) replaced by a LLU+ network wholesale input cost.

<u>Use of an alternative network input costs akin to the LLU+ cost by Eircom as its wholesale input in Larger Exchange Area</u>

5.27 The question arises as to whether Eircom should ever be allowed to use the price of LLU as an input to its net revenue test in the Larger Exchange Area. Clearly this would happen under the proposed weighting mechanism if 100% of all OAO lines were based on LLU. However, this is unlikely to occur in practice and consideration must be given as to whether Eircom should be constrained to price based on SB-WLR indefinitely. In considering where / when Eircom could use a LLU+ cost in the Larger Exchange Area, a number of considerations are pertinent:

5.27.1 The consideration of maintaining an economic space based on REO principles between indirect access services and LLU. Allowing Eircom to use LLU+ as an input into its bundles risks causing a margin squeeze for users of indirect access services in the Larger Exchange Area.

5.27.2 Where the Larger Exchange Area as defined includes Area 3, consideration of the relevant input would be higher than the current maximum price of LLU since this maximum price largely reflects the costs of Areas 1 and 2 only.

5.27.3 The use of a sunset clause allowing the use of LLU+ arguably may spur migration to LLU in the short run. However, the timing of any such move would be important as OAOs would need to have time to plan and ComReg would need to be sure that LLU had rolled out to an adequate degree in that area.

5.27.4 The benefit to retail end-users in allowing Eircom to use a LLU+ wholesale input to offer cheaper bundles.

5.28 Therefore, ComReg seeks views as to the appropriateness of a sunset clause and views on where/when LLU+ could be used. This issue is considered in detail below:

Possible regulatory trigger mechanisms for use of an appropriate LLU+ in the net revenue test in the Larger Exchange Area as replacement to weighted average mechanism:

5.29 To decide when and where to utilise LLU+ as the wholesale input in the net revenue test in the Larger Exchange Area, ComReg could consider:

(1) <u>Explicit number of unbundled lines or explicit % of unbundled lines:</u>

There is a relevant UK precedent where the pricing of BT's WBA product (IP Stream) was tied with the number of local loops unbundled[38]. In addition to

[38] In the UK, alongside introducing a variety of regulatory modifications, Ofcom and BT established a threshold whereby when 1.5m LLU lines were installed adjustments in BT's bitstream prices were allowed. More specifically, in order to achieve price stability between LLU and IP Stream, BT committed to no further price changes until 1.5m LLU lines were installed; then a 75p per month reduction until April 2007 was introduced.

being a straightforward indicator of facilities-based competition, the attractiveness of this approach stems from its transparency. LLU penetration is monitored and the respective figures published regularly. The threshold based on the number of unbundled lines could be defined to be consistent with the forecasts inherent in the BU-LRIC model underlying the setting of maximum prices for Eircom's ULMP product under Decision D01/10.

ComReg recognises that a potential disadvantage of using an explicit number or percentage of unbundled lines as a threshold is that it could, in principle, incentivise entrants to avoid exceeding the threshold. However, ComReg believes this seems unlikely given that the business case of LLU is driven by scale. It is also in all operators' interests that the Eircom network as a whole is competitive and not constrained by artificially high wholesale prices in urban areas where other platforms may have much lower input costs.

ComReg also recognises that setting a simple and transparent target for LLU may provide Eircom with sufficient incentives to ensure that the processes associated with the provision of LLU comply with the standards required. The increased take up of LLU by operators and by consumers of their offers is a reasonable indicator that OAOs are being treated in a non discriminatory way and that the wholesale reform process is working. This has not been the case in the past where OAOs have claimed that LLU was too expensive relative to the price of other resale wholesale products and too clunky a process to work for OAOs.

If a target is set, ComReg believes that it must be consistent with current assumptions made in current pricing models in relation to LLU and WBA and must reflect the current prevailing market situation and realistic future projections.

(1b) <u>LLU Line Multiplier:</u>

Linked to 1 above, an option could be to use a weighting of LLU lines to total lines but to give LLU lines a multiplier effect, for example, an LLU line is weighted to be, say, 5 times a SB-WLR line. Therefore, for example, with the use of a LLU Line Multiplier of 5, 200,000 LLU lines unbundled would be the equivalent of 1 million SB-WLR lines. This approach recognises that a successful LLU line take-up will be a fraction of national SB-WLR take-up.

(2) <u>Number of operators present in an exchange:</u>

An alternative, and potentially supplemental, method of determining a threshold would be to base it on the number of operators in an exchange in the Larger Exchange Area. This approach could also be used to determine where the net revenue test based on LLU+ could be used. In this respect, it can be noted that both LLU and cable have focused on certain densely populated regions to date.

(3) <u>Competitive assessment:</u>

ComReg recognises that approaches (1) and (2) above may be unfair to Eircom, in the context of potentially emerging competition from alternative platforms, for example cable, by making it wait for a sufficient take-up of LLU to allow it utilise LLU+ as the applicable wholesale input. Furthermore, near-term investments in NGA may be impacting the business case for LLU take-up. However, ComReg recognises that Eircom might at some stage be allowed utilise an appropriate network input akin to the LLU+ to reflect the cost of unbundling the area addressed and use this as the applicable wholesale input in the net revenue test in order to compete in those areas where there is evidence of LLU competition / cable competition.

(4) Time based approach:

ComReg acknowledges, however, that there may be a view by Eircom that it should not be impeded from competing or from offering cheaper packages to consumers where an LLU operator has failed commercially to achieve sufficient market share. Where such a failure cannot be attributed to discriminatory behaviour by Eircom, there may be a case for allowing Eircom use the LLU+ / network input cost in the net revenue test in certain areas so as to offer cheaper bundles to end users. Therefore, ComReg seeks respondents' views as to whether a time based approach be applied - for example using the weighted average wholesale input from April 2012 (if the resultant Direction following this consultation is made in March 2012) for a period of six months with a move to use an input based on LLU+ approximately a year from the date of this paper – Autumn 2012. ComReg seeks views as to whether this wouldallow the market to develop sufficiently and allow OAOs sufficient time to revise their business strategy if required.

ComReg seeks views as to whether it might be appropriate to move to an input of a LLU+ / network input cost only in the net revenue test for any Area(s) of Figure 4 at this time. If not, ComReg seeks respondent's views as to the appropriate trigger for when the LLU+ input might be used. ComReg also seeks views as to within what Area(s) of Figure 4 this could be done

NGB area and ULMP maximum price

5.30 The price of ULMP is subject to a cost orientation obligation under Decision D05/10 and is currently set at a maximum price of €12.41 based on 149 exchanges. Therefore, this ULMP price is based on fewer exchanges than the number of NGB / BMB exchanges of c.250. Therefore, there may be an argument that the use of LLU+ as a wholesale input should be limited to those exchanges assumed in the LLU price control model (Area 1 – 2 of Figure 4) and should not apply across the entire NGB footprint (Area 1 – 3 of Figure 4) — or if it is to apply, a higher LLU input price should be used to reflect the cost of unbundling all the NGB / BMB exchanges. The current ComReg LLU price control model, a copy of which Eircom has, can calculate the costs of unbundling beyond the 149 exchanges that were assumed to be unbundled. This is based on the BU-LRAIC model adopted in Decision D01/10. The BU-LRAIC model methodology was consulted on in 2008 and set out in ComReg Document No. 09/39. ComReg would welcome views on this.

Q. 2. In defining the Larger Exchange Area where a different wholesale input may be allowed, what area(s) of Figure 4 do you believe should be included in the Larger Exchange Area? Do you agree or disagree with the proposed use of a weighted average wholesale input in the net revenue test in the Larger Exchange Area? When / what area(s) of Figure 4 do you consider it would be appropriate for Eircom to be allowed use a LLU+ network input cost in the net revenue test in the Larger Exchange Area? Please give a detailed response with supporting data where appropriate to support your view.

6 Application of the proposed revised net revenue test under Decision D07/61

6.1 Based on the proposals / preliminary views of Chapter 4 and 5, the following is the application of the proposed revised net revenue test under Decision D07/61 where these proposals are decided on following consideration of responses to this consultation and other available evidence: (NOTE: for the purposes of this Chapter 6, "bundle" means a package of services, consisting of retail fixed narrowband access and one or more other services, which is offered for sale by Eircom to end users.)

REF	**ITEM (all ex VAT)**	**Description**	
	Revenue:		
R1	Monthly Bundle Price	This is the headline monthly price of a bundle.	
R2	Monthly Out of Bundle Calls Revenue	This is a weighted average of the total calls revenue earned on average outside the bundle per month based on actual revenues and volumes (post-launch assessment) or forecast revenues and volumes (pre- launch assessment). This is calculated for each component call that is charged separately outside the bundle by: (i) taking the total number of calls for that component that are outside by bundle allowance and multiplying that by the call set up fee; and (ii) taking the total minutes for that component that are outside bundle allowance and multiplying that by the retail price per minute. This total revenue for the component outside bundle allowance is then divided by the total number of customers to get an average revenue per customer for that component used outside of bundle allowance.	
R3	Monthly Out of Bundle Other Revenue	This is the average of any other monthly out of bundle revenue.	
R4	**Total Monthly Bundle Revenue**	**This is the sum of the Monthly Bundle Price *plus* Monthly Out of Bundle Calls Revenue *plus* Monthly Out of Bundle Other Revenue.**	
R5	**Total Monthly Portfolio Revenue**	**This is a weighted average of Total Monthly Bundle Revenue based on the actual volumes of each Bundle in the Portfolio (in the case of post-launch assessment) or the forecast volumes for each Bundle in the Portfolio (in the case of pre-launch assessment).**	
	Costs:		
C1	Total Wholesale Access Input Cost	In the case of Bundles sold from the Larger Exchange Area	This is the applicable monthly prices plus all relevant wholesale costs of SB-WLR, WBA, Line Share and LLU network input cost in effect in the Larger Exchange Area weighted by the use of those wholesale inputs by OAOs in the Larger Exchange Area. In this context "all relevant wholesale costs" means a) ancillary charges levied by Eircom in respect of a particular service amortised, where appropriate, over the relevant assumed customer life[39] plus b) other unavoidable non-retail costs which are necessary to provide a retail service[40]. All costs are converted to a monthly average.

[39] For example, connection fees or co-location charges

[40] For example, the cost of a line card, amortised over the relevant customer life

		In the case of Bundles sold from outside the Larger Exchange Area	This is the sum of the monthly prices of SB-WLR and WBA plus the monthly average of all relevant wholesale costs levied by Eircom.
C2	Retail Costs Associated with Retail Line Rental	These are the monthly operating costs as derived from the SB-WLR regulated retail minus price control.	
C3	Mailbox cost	Where the bundle packages include free mailbox, the wholesale monthly price of the mailbox as per the regulated retail minus price control as published in Eircom's Reference Interconnect Offer Price List must be taken to ensure an operator can replicate the offer. However, consideration will be taken of the applicable average take up of the mailbox and the wholesale price will be adjusted to reflect this. The retail costs as derived from the retail minus price control will also be considered here.	
C4	Total Cost of Calls	These are the monthly weighted average of the wholesale and retail costs as calculated for each retail call including all common cost. Costs are based on wholesale prices and Eircom's retail costs according to its latest regulatory accounts to derive an average total cost and will reflect known future changes in those costs where these can be adequately verified.	
C5	Total LRIC of Calls	This is estimated from Eircom's accounts as Total Cost of Calls *less* common costs *less* fixed indirect costs (LRIC of retail calls only)	
C6	Retail Costs Associated with Retail Broadband	These are the monthly operating costs as derived from the WBA regulated retail minus price control.	
C7	**Total Bundle Cost**	**This is the Total Wholesale Access Input Cost *plus* Retail Costs Associated with Retail Line Rental *plus* Retail Costs Associated with Retail Broadband *plus* Total Cost of Calls *plus* the LRIC of unregulated retail services *plus* Mailbox Cost where applicable**	
C8	**Total Monthly Adjusted Bundle Cost**	**This is the Total Wholesale Access Input Cost *plus* Retail Costs Associated with Retail Line Rental *plus* Retail Costs Associated with Retail Broadband *plus* Total LRIC of Calls *plu*s the LRIC of unregulated retail services *plus* Mailbox Cost where applicable**	
C9	**Total Monthly Portfolio Cost**	**This is the weighted average by volume of Total Bundle Cost based on actual monthly volume for each Bundle in the Portfolio (in the case of post-launch assessment) or the forecast monthly volume for each Bundle in the Portfolio (in the case of pre- launch assessment).**	

Assessment of Bundles:

In order to pass the Net Revenue Test:

(i) as regards every Portfolio, the Total Monthly Portfolio Revenue shall be equal to or exceed the Total Monthly Portfolio Cost;

(ii) as regards each individual Bundle, the Total Monthly Bundle Revenue shall be equal to or exceed the Total Monthly Adjusted Bundle Cost;

(iii) when a given Bundle includes unregulated retail services, compliance with the Net Revenue Test (as regards such unregulated services) shall be evaluated in accordance with the Unregulated Retail Services Assessment set out below.

Unregulated Retail Services Assessment
This applies to those retail services that are unregulated and do not rely on retail fixed narrowband access. The incremental revenues over the average customer lifetime (which can be different for different unregulated products) of any unregulated product in a Bundle must cover its own long-run incremental costs ("LRIC") including applicable retail costs. For mobile services, the aggregate revenue of all the respective unregulated services offered by Eircom must cover the respective Long Run Average Incremental Cost plus common costs ("LRAIC+") of those products e.g. the aggregate revenue of E-Mobile voice services must cover its own LRAIC+. There must be no cross-subsidisation between regulated services and unregulated services. On a case-by-case basis where the bundling of the unregulated service will not have a significant impact on competition, ComReg will consider allowing that unregulated service only cover its own avoidable costs ("AAC") instead of its LRIC. In the absence of any robust LRAIC+ / LRIC data, ComReg will use the standalone price of that unregulated service in the test on the basis that the standalone price recovers the long-term cost of the product or any other proxy / benchmark for long-term cost that ComReg considers is appropriate.

Unreasonable Bundle Assessment
If a Bundle does not pass the Net Revenue Test, as outlined in Section 4.3 of the Draft Direction, ComReg will carry out a general assessment of the reasonableness of the Bundle and may conclude that, notwithstanding the fact that the Bundle fails the Net Revenue Test, the offer for sale by Eircom of that Bundle does not constitute a breach of the obligation under ComReg Decision D07/61 not to unreasonably bundle services. For the purposes of such assessment, ComReg may, in particular, have regard to any robust evidence of retail efficiencies or increased customer lifetimes resulting from the relevant Bundle. ComReg will also consider the impact of the Bundle on competition, including by reference to the promotion of sustainable competition in the medium to long term and the likelihood of any potential foreclosure and associated consumer harm.

ComReg's preliminary views on the net revenue test to assess whether a bundle is unreasonable pursuant to D07 / 61

6.2 In summary, given developments in the telecoms sector in Ireland generally and the regulatory objectives behind the obligation not to unreasonably bundle, it is proposed that the net revenue test be now further specified as follows:

6.2.1 The net revenue test is a two part test: Part 1 - an assessment of relevant portfolios of bundles on an ATC cost recovery basis; Part 2 an assessment of individual bundles with a lower LRIC cost standard for retail calls.

6.2.2 In relation to setting the portfolios of bundles for the Part 1 test, it is proposed that Eircom's current and future set of retail bundles can be categorised into the following two aggregate bundle portfolios: (1) Bundles sold from within the Larger Exchange Area; (2) Bundles sold from outside the Larger Exchange Area.

6.2.3 ComReg seeks views on formulating the Larger Exchange Area. It could refer to only Areas 1 - 2 of Figure 4 or it could refer to Areas 1 – 3 of Figure 4.

6.2.4 ATC can reflect known future changes in wholesale costs and retail costs e.g. MTR reductions.

6.2.5 Currently, the net revenue test is based on 'resale' wholesale inputs of WBA (Bitstream) and SB-WLR. ComReg now proposes that this approach remains only for bundles in Portfolio 2, that is, bundles sold from outside the Larger Exchange Area. For Portfolio 1, that is bundles sold from within the Larger Exchange Area, it is proposed that a weighted average wholesale input cost would be used.

6.2.6 In relation to unregulated products and services (e.g. IPTV, mobile voice, mobile broadband), ComReg proposes that an unregulated product, such as mobile voice, must cover its own Long Run Incremental Cost ('LRIC') and the aggregate of all applicable unregulated products (i.e. all the mobile voice offers) must recover the Long Run Average Incremental Cost plus common costs ('LRAIC+') of the mobile voice service over the relevant network. Also, there must be clear evidence that no cross-subsidisation between the regulated markets and the markets for the unregulated products and services. Such evidence will be gathered through the annual regulated accounts review. The 2010/11 Eircom Regulatory Accounts are prepared in line with ComReg Decision D08/10 for the first time. Under that decision, ComReg will gather sufficient information to ensure the profits/losses on regulated products and services and unregulated products and services where necessary are submitted to ComReg by Eircom annually. On a case-by-case basis, ComReg could consider the use of Average Avoidable Costs ('AAC) for unregulated products and services where it is clear that the medium to long-term competition in the market generally would not be harmed and that it would not create material distortions to competition through anti-competitive practices stemming from SMP products and services.

6.2.7 It is proposed that the net revenue test will be complemented by an assessment of the competitive context of the bundle and the test would not change when a bundle is claimed to be a response to a competitor's bundle, when a bundle is found to be unreasonable post launch or if a bundle is a promotion. This would apply both to individual bundle assessments and portfolio bundle assessments.

Q. 3. Do you agree or disagree with the proposed revised net revenue test? Please give a detailed response with supporting data where appropriate to support your view.

7 Notification, pre-clearance, modification / withdrawal of retail bundles that include Retail Fixed Narrowband Access

7.1 As noted in Consultation Document No. 10/01, as part of the 2009 settlement agreement, Eircom is not permitted to launch bundles which include line rental without ComReg's prior approval, which ComReg would not unreasonably withhold or delay. Furthermore, on the basis of two consecutive data sets that show a bundle is unreasonable, Eircom must modify / withdraw such bundles within two months.

7.2 As that settlement agreement will no longer apply once a Direction following this consultation is in effect, ComReg, as noted in Consultation Document No. 10/01, proposes to further specify the notification, pre-clearance, modification / withdrawal of bundles that include retail fixed narrowband access services pursuant to D07/61.

7.3 ComReg remains of the view that the proposals in Consultation Document No. 10/01 remain largely appropriate. Annex D examines respondents' views to Consultation Document No. 10/01 and sets out ComReg's position. However, having considered the views of respondents, ComReg proposes three changes from the preliminary position of Consultation Document No. 10/01:

7.3.1 ComReg proposes to review Eircom's pre-notification submission within five working days instead of ten working days. This revised proposal allows Eircom to get new or revised bundles into the market as quickly as possible. However, ComReg also has the ability to request more time if required – therefore, for new / complex bundles it would be in Eircom's interest to ensure that enough time is given to ComReg in order to allow ComReg to review the bundle before the planned launch date set by Eircom. ComReg considers that it is not in Eircom's or ComReg's or, most importantly, consumers' interests to allow a bundle into the market which subsequently has to be modified / withdrawn as ComReg's review pre-launch was not given enough time. However, ComReg assumes that Eircom would have undertaken a rigorous internal review to ensure compliance before any such notifications to ComReg.

7.3.2 Upon ComReg informing Eircom of its view that a bundle is unreasonable, Eircom must immediately stop offering or selling that bundle to additional customers. This ensures that the adverse affect on the market is ceased immediately once a bundle is found to be unreasonable.

7.3.3 ComReg proposes to increase by two weeks, to twelve weeks, the required time for Eircom to modify / withdraw any unreasonable bundle as this should allow Eircom sufficient time to deal with existing customers on the unreasonable bundle and, in particular, recognises the notification timelines associated with any changes to retail and wholesale products - any change to SB-WLR requires a two month notification to ComReg.

7.4 These proposals are set out in the draft Direction at Annex B and are discussed below.

<u>Notification and pre-clearance</u>

7.5 ComReg is of the preliminary view that prior to the date that a new bundle that includes retail fixed narrowband access is to be made available or offered for sale by Eircom, that Eircom should furnish to ComReg a detailed written submission demonstrating the bundle's compliance with the obligation not to unreasonably bundle (including passing the net revenue test). The submission would make full and true disclosure of all material facts for the purpose of demonstrating compliance with the obligation not to unreasonably bundle. In the submission, all assumptions would be clearly set out together with the rationale and supporting evidence for such an assumption and the likely effect if an assumption is not met. The net revenue test workbook presented would be capable of running scenarios for changed key assumptions and this must be kept up to date by Eircom. Any claims for retail efficiencies / increased customer lifetimes should be supported by robust evidence. Upon receipt of the submission, ComReg would review the submission and within five working days, give or withhold approval for launch of the proposed bundle that includes retail fixed narrowband access — such approval would not be unreasonably withheld and Eircom may not launch the bundle without having received such approval from ComReg.

7.6 It is proposed that, within the five working day period, ComReg may seek further information in order to inform its decision whether approval to launch should be given or withheld – if the further information is not provided within ComReg's timeline or to the standard required by ComReg, approval could be withheld pending the required information being available to ComReg for review and consideration. ComReg seeks respondents' views as on the preliminary views expressed above.

Preliminary view: Eircom must notify and obtain approval for bundles that include retail fixed narrowband access at least five working days before launch.

Modify / withdraw non-compliant bundles within twelve weeks

7.7 Where a bundle that includes retail fixed narrowband access is launched and in the market, Eircom must at all times ensure it meets it regulatory obligation not to unreasonably bundle. Therefore, Eircom must notify ComReg immediately together with supporting evidence if it believes that any such bundle may have become unreasonable. Also, if requested by ComReg at any time, Eircom should provide such data as may be requested by ComReg for the purposes of verifying Eircom's ongoing compliance with the obligation not to unreasonably bundle services. In this submission Eircom should also provide any other relevant information it believes is required so that ComReg can make an informed decision as to whether the bundle is compliant with the obligation not to unreasonably bundle and whether Eircom is meeting its regulatory obligations.

7.8 ComReg is of the preliminary view that if on the basis of its review of not less than two consecutive net revenue test data sets, complemented by an assessment of the competitive context of the bundle in question, ComReg is of the view that a bundle that includes retail fixed narrowband access amounts to unreasonable bundling, ComReg will inform Eircom in writing of such view. ComReg proposes that, upon receipt of that view Eircom should immediately cease the addition of any retail consumers to the designated unreasonable bundle and within twelve weeks modify or withdraw that bundle. If a bundle is unreasonable, ComReg's preference is for modification of wholesale inputs to make the bundle reasonable. If Eircom does not wish to withdraw the bundle, Eircom could potentially, by way of example, propose to modify the bundle as follows:

(i) Reduce the price of the wholesale inputs mindful of the need to maintain an appropriate economic space between the relative prices of wholesale products;

(ii) Reduce the price of the retail line rental below the regulated maximum price;

(iii) Any other corrective action that is mutually agreed by ComReg and Eircom; or

(iv) A combination of the above.

7.9 ComReg is of the preliminary view that such proposed modifications to the bundle by Eircom should be notified to ComReg at least one week prior to the expiry of the proposed twelve week deadline. In notifying ComReg to meet the twelve week deadline, Eircom shall be cognisant of any other regulatory notification requirements it may have, including its regulatory obligation to notify retail customers of any proposed contract changes and to notify OAOs of any proposed change to the price of SB-WLR[41].

Preliminary view: Eircom must withdraw / modify any unreasonable bundle that includes retail fixed narrowband access within twelve weeks – this is an increase from the ten week proposal of Consultation Document No. 10/01. Within that twelve-week period, Eircom must not add any customers to the relevant bundle until and unless such bundle is modified to ComReg's satisfaction.

Q. 4. Do you agree or disagree with the pre-notification and pre-clearance requirements for bundles that include retail fixed narrowband access? Please explain your response and provide detailed information to support your view.

Q. 5. Do you agree or disagree that if ComReg is of the view that a bundle in the retail fixed narrowband access market is unreasonable that Eircom should modify / withdraw such bundle within twelve weeks? Please explain your response and provide detailed information to support your view.

[41] See for example 6.12 of Decision Instrument D07/61 – Eircom must notify ComReg two months in advance of change

8 WPNIA – further specification of obligation not to margin/price squeeze

8.1 Currently, in addition to its obligation of cost orientation, Eircom has a regulatory obligation not to cause a margin/price squeeze in connection with the WPNIA market[42]. As noted in the WPNIA market review, Eircom must ensure that "*the relationship between its wholesale and retail pricing, and <u>between the pricing of its wholesale products</u>, does not constitute a margin squeeze.*"[43] (<u>emphasis added</u>). This chapter will examine what is the appropriate relative margin between Eircom's ULMP product and:

(i) its SB-WLR product;

(ii) its Naked WBA ("NWBA") product (when available).

8.2 ComReg considers that preserving a sufficient economic space between different wholesale inputs offered by Eircom is necessary so as to promote and foster sustainable and effective competition in the provision of retail services to end users. ComReg considers that from a regulatory perspective it is important that the economic space between these different wholesale products or "rungs" on the ladder of investment is sufficient to promote the development of effective retail competition capable of constraining the integrated incumbent on an ongoing and sustainable basis. ComReg believes that in the absence of an appropriate price control maintaining such an economic space, Eircom, by virtue of its control of the underlying access infrastructure and its presence at both wholesale and retail levels, would have the ability and incentives to price its wholesale access inputs in such a way as to dampen the competitive constraints it faces at the retail level and to ultimately extract more profits through higher retail prices for consumers.

8.3 ComReg considers that this notion of preserving a sufficient economic space is a clear and widely accepted concept and is entirely consistent with ComReg's statutory objectives of promoting competition, encouraging efficient investment in infrastructure and promoting innovation, as well as safeguarding the interests of end users.

8.4 For example, in European Commission Decision of 04.07.2007 relating to a proceedings under Article 82 of the EC Treaty (Case COMP/38.784 – Wanadoo España vs. Telefónica), the European Commission, when assessing the replicability of Telefonica's retail prices, noted that the process of climbing of the ladder of investment can only be effective if there is a margin between all the steps of the ladder.

8.5 Also, the ERG in its "ERG Report on price consistency in upstream broadband markets"[44], specifically recognises a possibility for regulatory action where there may be a price squeeze between two wholesale services (e.g., between mandatory WBA and other forms of bitstream access or resale). For example it notes: "*The need to maintain the coherence of the regulatory scheme may justify intervention with regard to non-regulated WBA offers, if the price unilaterally set by the SMP*

[42] Pursuant to s.12.4 of D05/10

[43] At para 7.128 of Decision D05/10

[44] 09 (21) dated June 2009

operator is so attractive that in practice it reduces the incentives of alternative operators to invest in alternative means of access that would enable further differentiation from the incumbent's offers. This will be particularly true in cases where the conduct pertaining to a non-regulated WBA offer has distorting effects over the policy objectives set by the NRA for alternative operators to climb the ladder of investment (including creation of economic spaces between wholesale services)."[45]

8.6 Currently there is no regulatory floor for either the price of SB-WLR or NWBA. ComReg's objective in this chapter is to provide assurance to LLUOs that neither the pricing of SB-WLR (especially sold in combination with WBA) nor NWBA will be priced at an excessively low level such that LLUOs will be foreclosed.

8.7 Consequently, in this consultation, we are proposing to further specify the obligation under Decision D05/10 not to cause a margin/price squeeze for the WPNIA product, ULMP, based on a REO. This is consistent with the approach of Consultation Documents No. 10/56 and 10/108 which were to minimise the risk of a margin/price squeeze to the WPNIA product LLU Line Share[46]. The proposal contained in this chapter should minimise the risk of Eircom squeezing those operators who have invested to avail of ULMP by setting its relative prices of other wholesale products too low, in particular:

8.7.1 Setting the price of its SB-WLR product too low relative to its pricing of its ULMP product

8.7.2 Setting the price of its Naked WBA (Bitstream) DSL product too low relative to the pricing of its ULMP product. In particular, ComReg Decision D05/10 noted that:

"*ComReg's objective here is to encourage efficient infrastructure-based competition, and we recognise that this objective could be undermined if the relationship between the WPNIA price and the WBA price distorts incentives to invest and operate in the WPNIA market. At present, the concern is between LLU pricing and bitstream pricing. Therefore, ComReg wishes to establish a principle that will maintain an economic space between WPNIA and WBA pricing.*"[47]. Furthermore, in the recent WBA market review, ComReg noted:

"*In assessing Eircom's belief that we have not justified the need to maintain an appropriate economic space between prices set for WBA and prices set for WPNIA, we note that this issue was raised as a potential example of leveraging, where the SMP operator may seek to foreclose infrastructure-based competitors by way of maintaining an insufficient economic space between the relative pricing of different upstream/intermediate inputs. We explained that, absent regulation, a dominant operator could potentially use its dominance to "game" the system – for instance, by making the wholesale product which is least attractive or profitable for them, or which could pose the greatest competition risk over the longer term, unattractive to OAOs through higher relative prices or degraded service. Our view was that absent*

[45] At page 25

[46] See Consultation Document No. 10/108

[47] Para 7.182 of ComReg Document No. 08/104 which forms part of D05/10

regulation, Eircom would have the ability and incentive to price its wholesale inputs in a way that increases uncertainty and could dissuade potential entrants from engaging in efficient infrastructural investments. This is possible because Eircom is active in a number of related input markets. … our view is that there is clear justification for establishing that a failure to maintain an appropriate economic space between WBA and WPNIA prices would constitute a competition problem and that we are therefore justified in imposing an obligation to remedy this."[48]

8.7.3 Setting the LLU+ input too low in the net revenue test where use of this input is appropriate in the Larger Exchange Area.

8.8 Therefore, this chapter will set out a proposed Margin/Price Squeeze Test in the WPNIA market which it is proposed will be used to calculate the appropriate minimum price floor for the ULMP component in a SB-WLR product or a Naked WBA (Bitstream) DSL product.

8.9 ComReg's aim, in setting this Margin/Price Squeeze Test, is to promote competition by ensuring that operators have appropriate incentives to invest efficiently in infrastructure so that they become less reliant on the incumbent's network. Without an appropriate price floor to minimise the risk of squeezing WPNIA, operators may not invest / increase their investment in WPNIA and may stay on resale wholesale products from Eircom. This would benefit Eircom as operators that remain on resale wholesale products have less potential to offer differentiated retail products, possibly at lower prices and must continue to pay higher wholesale charges to Eircom.

Appropriate Wholesale Network Input cost in the Margin/Price Squeeze Test

8.10 NWBA by definition provides the entire suite of services offered to the end user which implies that the full cost of a local loop, appropriately defined, would need to be recovered in its price.

8.11 Currently under Decision D01/10 narrowband channels where used (i.e. when WLR or retail narrow band access is provided) recover all the common cost of the local access network.

8.12 In setting a price floor for NWBA and SB-WLR, in order to minimise the risk of a margin/price squeeze to ULMP, a key consideration is what part of the network to take account of. This would be used to derive a Wholesale Network Input ("WNI") cost in the Margin/Price Squeeze Test.

8.13 In the first instance it would appear that as unbundling is very unlikely to take place in Areas 4 and 5 of Figure 4 as described above that including the cost of loops in these areas as part of a floor would be excessively inflexible and would potentially deprive consumers in these areas of the benefits of lower prices.

8.14 On the other hand if one believes that only Areas 1 and 2 (149 exchanges) are susceptible to unbundling then a WNI would be based on the costs of the local access network in these areas only. The current price of LLU (€12.41 per month) is a good proxy for these costs.

[48] Para 6.11 of Decision D06/11

8.15 Finally, and assuming that NWBA will be available in a footprint corresponding to Eircom's NGB platform, a measure of cost consistent with the model used to calculate the price of LLU but covering this larger footprint may be appropriate. This would mean that a WNI would be calculated by reference to Areas 1, 2 and 3 of Figure 4.

8.16 ComReg invites views as to what is the most appropriate input to a WNI for the purposes of setting an appropriate price floor for WLR and NWBA.

Margin/Price Squeeze Test in WPNIA market set by reference to a REO

8.17 As already set out in paragraph 5.21 of this consultation and reproduced below, ComReg proposes that LLU+ will be used to calculate the appropriate minimum price floor for the ULMP component in a SB-WLR product or a Naked WBA (Bitstream) DSL product, and will be set by reference to a REO by including the following:

8.17.1 The appropriate WNI cost.

8.17.2 The cost of fault clearance per month. ComReg calculates this as €0.81 a month based on average 8% faults for a REO LLU operator. ComReg used the 8% fault rate in the setting of the ULMP price as a proxy for an efficient new network operator in the 149 exchanges.

8.17.3 The cost of ULMP connection fee and ULMP disconnection fees over an average customer lifetime of 42 months for the number of customers in the model.

8.17.4 The appropriate cost of a line card if any. The line card has to date facilitated PSTN calls over Eircom's network. However, with the introduction of voice over broadband and other technologies it may no longer be necessary to include this part of the network in the underlying costs borne by Eircom of maintaining the line card. ComReg would welcome submissions in this regard.

8.17.5 The cost of DSLAM related costs and Transport costs will be informed by the minimum price floor model for WBA which was consulted on in Consultation Document No. 10/108 and is subject to finalisation based on responses to that consultation. ComReg requested information from OAOs for these costs previously for that consultation and, where appropriate, this information has been used by ComReg to finalise the WBA minimum price floor model – ComReg intends to issue a Decision on this in the near future. The costs included are described in Consultation Document Nos. 10/56 and 10/108 and include fixed and common costs of a typical LLU operator together with a rate of return on the capital equipment of 10.21%, the Weighted Average Cost of Capital ('WACC') currently applied to Eircom.

Possible illustrative structure of "Margin/Price Squeeze Test" in the WPNIA market to minimise the risk of a margin/price squeeze to ULMP assuming Areas 1 and 2 of Figure 4 form the basis of the WNI:

WNI cost [**149** exchanges] – if Area 1 and 2 only	€12.41
ULMP Fault Repair [149 exchanges] (€117.31*8%) / 12 [Actual fault repair cost * fault % used in ULMP price control model]	€0.81
Line card (included in DSLAM)	€0.00
ULMP connection and disconnection charges	€0.90
Total possible minimum price floor for ULMP component in SB-WLR excluding line card cost (if appropriate)	**€14.12**
Where broadband included: use WBA minimum price floor model:	
DSLAM costs [based on current DRAFT of minimum price floor model for WBA – subject to finalisation]	€6.88
Transport costs [based on current DRAFT of minimum price floor model for WBA – subject to finalisation]	€3.75
Total possible minimum price floor for ULMP component in Naked WBA DSL	**€24.75**

8.18 <u>ComReg would welcome views on this proposed Margin/Price Squeeze Test in the WPNIA market based on a REO to minimise the risk of a margin/price squeeze to ULMP, and particularly as to whether all costs have been considered and included in the above possible illustrative structure.</u>

Q. 6. Do you agree or disagree with ComReg's proposed REO test to minimise the risk of a margin/price squeeze to ULMP? Please explain your response.

Q. 7. In your opinion, how should the cost of the network be calculated for setting the Wholesale Network Input ("WNI") for the purposes of the proposed WPNIA margin/price squeeze test to minimise the risk of a squeeze on ULMP? Please explain your response.

9 WBA – possible further specification of obligation not to margin/price squeeze

9.1 While previous ComReg consultations in relation to retail bundles were focused on the Retail Fixed Narrowband Access Markets, recent developments in the markets have made it clear that the bundled sale of regulated and unregulated services will not always include retail fixed narrowband access. For example, more OAOs are considering the sale of Retail SAB/Naked DSL where customers will be given the option to forego the option to use the PSTN network as has traditionally been the case for fixed voice calls. Therefore, the obligation not to unreasonably bundle may no longer apply to such bundles. However, in view of Eircom's SMP in the related WBA market and its integrated position into the retail markets, the threat of anti-competitive behaviour through leverage remains and, therefore, the regulatory framework needs to address such bundling of services.

9.2 Therefore, this chapter concerns proposals related to the existing obligation not to margin/price squeeze in the WBA market pursuant to D06/11. ComReg is seeking views as to whether this existing obligation should be further specified to include a margin/price squeeze test in the WBA market. In particular, this proposed test in WBA would deal with bundles including the wholesale equivalent of Retail SAB/Naked DSL to ensure that OAOs are not squeezed at the retail level where Eircom avails of Naked WBA (Bitstream) DSL. It should be noted that this discussion is in the context of a copper only access network. ComReg's forthcoming consultation on the regulation of NGA will address similar issues in that context. ComReg will consider responses to that NGA consultation also before proceeding further.

9.3 The chapter also seeks views as to whether the existing D01/06 margin squeeze test in the WBA market should be amended from the basis of SEO to EEO.

Should there be a margin/price squeeze test for bundles that include WBA/Naked WBA DSL?

9.4 As stated above, ComReg is seeking views as to whether the existing obligation under Decision D06/11 not to cause a margin/price squeeze should be further specified to include a margin squeeze test in the WBA market. Currently, retail bundles that include WBA are subject to the provisions of ComReg Decision D01/06 but this Decision will be reviewed later in 2012 with a proposal to use a cost based price control to set the maximum price of WBA. However, ComReg considers that, without an appropriate price control, there is a risk of Eircom masking its effective retail price for broadband and implementing a price squeeze vis-a-vis WBA when sold as part of a broader retail package potentially incorporating (fixed/mobile) calls, TV, etc. ComReg considers that such anti-competitive behaviour could render the WBA input ineffective and, given that retail broadband competition still depends to a significant degree on the effective provisioning of WBA, this could have significant negative implications for the structure of retail broadband competition where Eircom still has an influential presence (i.e. leveraging concerns).

9.5 In this context, the proposed margin squeeze test relates to a regulated WBA wholesale price against an unregulated retail price. As the European Commission states in its Explanatory Note[49] to the 2007 Recommendation on relevant product and service markets susceptible to ex ante regulation, "*when there is regulation at wholesale and/or retail level, the possibility of price or margin squeezes can result from regulatory intervention and it should be assessed in that context… For the assessment of a margin squeeze it is irrelevant whether both wholesale and retail prices are regulated or only one of the two. The relevant questions in this context are (i) whether the spread between wholesale and retail prices cover the retail costs of the dominant firm and (ii) whether the dominant firm is free to avoid the margin squeeze on its own initiative.*" (emphasis added).

9.6 As part of its analysis of the WBA market[50], ComReg identified competition problems, in particular the possible leverage of market power by Eircom in the WBA market into the downstream retail market for broadband products, by way of a margin squeeze.

9.7 The recent market review noted the continued reliance of retail broadband competition on the availability of effective WBA inputs:

"…DSL continues to account for the majority of retail fixed broadband subscriptions, standing at 66% of fixed broadband subscriptions (excluding WPNIA-based supply which as noted above accounted for a further 5%), as of Q1 2011. This shows that retail broadband competition still continues to rely significantly on the availability of regulated WBA inputs"[51]

9.8 The recent market review also noted:

"*Eircom is a major provider of retail broadband, and so is in a strong position to consolidate its position in the upstream WBA market as the primary supplier. Absent regulation, there would also be an incentive for such an integrated operator to reinforce entry barriers across the wholesale and retail broadband access markets, by, for example, applying a margin squeeze between wholesale costs and retail prices.*"[52]

9.9 The existing D01/06 price control in WBA applies to WBA standalone and when offered in bundles. However, as stated earlier, this price control may be removed in the near future. Consequently, for this reason and for the reasoning set out in the recent market review, ComReg believes that Eircom's ex-ante regulatory obligation not to margin/price squeeze could be further specified to include a margin squeeze test. ComReg believes it could be necessary to apply a similar margin squeeze test in the market of WBA in view of the continued importance of WBA to the competitive balance of the retail broadband market. This possible margin squeeze test would be to ensure that OAOs that purchase WBA from Eircom are not squeezed by Eircom offering that WBA/Naked WBA in retail bundles. It minimises

[49] Explanatory Note - Accompanying document to the Commission Recommendation on relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services, SEC (2007) 1483 final

[50] ComReg Document No. 11/49 (Decision D06/11) dated 8 July 2011

[51] Para 3.60 of ComReg Document No. 11/49 (Decision D06/11) dated 8 July 2011

[52] Para 6.54 of ComReg Document No. 10/81 dated 1 October 2010

this risk by taking the actual WBA/Naked WBA price charged by Eircom on OAOs in the test, which is a test of replication. Furthermore, this approach also ensures that where Eircom wishes to offer cheaper Retail SAB/Naked DSL, it must ensure that its wholesale equivalent offer remains appropriately priced[53] to match is retail offer price reduction sp as to minimise the risk of a margin/price squeeze.

9.10 As a proportionate measure, ComReg would consider the overall potential foreclosure effects of the margin squeeze in the marketplace so that compliance action may not be taken where ComReg considers that anti-competitive effects are not material. For example, where the margin squeeze test is failed in respect of a retail bundle of services incorporating WBA, ComReg will consider all available evidence on the competitive context of the retail bundle, similar to the assessment proposed in para 4.91 above. For example, relevant retail evidence would include an assessment of the nature and scope of the bundled offer and relevant complementarities across the bundle components, the level of broadband demand for retail bundles vis-à-vis the stand-alone elements, the ability to replicate such bundles, and any relevant commercial or strategic reasons for the bundled offer, etc.

9.11 Set out below, for discussion purposes, is a possible approach to this issue. ComReg considers that the retail costs below for the most part would likely reflect the retail costs used in a D07/61 net revenue test.

Possible Margin Squeeze Test Model for WBA / Naked WBA DSL:

REF:	**ITEM (all ex VAT)**	**Description**
	Revenue:	
R1	Monthly Bundle Price	This is the headline monthly price of a bundle. (NOTE: for the purposes of this Chapter 9, “bundle” means a package of services, consisting of the retail equivalent of WBA and one or more other services which is on offer or on sale by Eircom to end users.)
R2	Monthly Out of Bundle Revenue	This is the average of any other monthly out of bundle revenue[54].
R3	**Total Monthly Bundle Revenue**	**This is the sum of Monthly Bundle Price *plus* Monthly Out of Bundle Other Revenue.**
R4	**Total Monthly Portfolio Revenue**	**This is a weighted average of Total Monthly Bundle Revenue based on actual volumes for each Bundle in the Portfolio (in the case of post-launch assessment) or the forecast volumes for each Bundle in the Portfolio (in the case of pre-launch assessment).**
	Costs:	
C1	Wholesale Access Input Cost	This is the applicable NWBA/WBA price charged to OAOs *plus* a) ancillary charges levied by Eircom to OAOs in respect of NWBA/WBA amortised, where appropriate, over the relevant assumed customer life[55] *plus* b) other unavoidable non-retail costs which are necessary to provide a retail service. All costs are converted to a monthly average.
C2	Retail Costs Associated with	These are the monthly operating costs as derived from the WBA regulated retail minus price control.

[53] Eircom can price WBA/Naked WBA to the floors to be established which will ensure that there is no margin/price squeeze against WPNIA. See Chapter 10 for Naked WBA price floor proposal.

[54] This may include VOIP calls if charged separately

[55] For example, connection fees

	Retail Broadband	
C3	**Total Bundle Cost**	**This is the Total Wholesale Access Input Cost *plus* Retail Costs Associated with Retail Broadband *plus* the LRIC of unregulated retail services**
C4	**Total Monthly Adjusted Bundle Cost**	**This is the Total Wholesale Access Input Cost *plus* Retail Costs Associated with Retail Broadband *plus* the LRIC of unregulated retail services**
C5	**Total Monthly Portfolio Cost**	**This is the weighted average by volume of Total Bundle Cost based on actual volumes for each Bundle in the Portfolio (in the case of post-launch assessment) or forecast volumes for each Bundle in the Portfolio (in the case of pre-launch assessment).**

Possible assessment of Bundles in WBA:

It is proposed that in order to pass the obligation not to cause a margin/price squeeze:

(i) as regards every Portfolio, the Total Monthly Portfolio Revenue shall be equal to or exceed the Total Monthly Portfolio Cost;

(ii) as regards each individual Bundle, the Total Monthly Bundle Revenue shall be equal to or exceed the Total Monthly Adjusted Bundle Cost;

(iii) when a given Bundle includes unregulated retail services, compliance with the obligation not to cause a margin/price squeeze (as regards such unregulated services) shall be evaluated in accordance with the Unregulated Retail Services Assessment set out below.

Possible Unregulated Retail Services Assessment in WBA:

It is proposed that the following would apply to those retail services that are unregulated and do not rely on retail fixed narrowband access:

The incremental revenues over the average customer lifetime (which can be different for different unregulated products) of any unregulated product in a Bundle must cover its own long-run incremental costs (“LRIC”) including applicable retail costs.

For mobile services, the aggregate revenue of all the respective unregulated services offered by Eircom must cover the respective Long Run Average Incremental Cost plus common costs (“LRAIC+”) of those products e.g. the aggregate revenue of E-Mobile voice services must cover its own LRAIC+.

There must be no cross-subsidisation between regulated services and unregulated services.

On a case-by-case basis where the bundling of the unregulated service will not have a significant impact on competition, ComReg will consider allowing that unregulated service only cover its own avoidable costs (“AAC”) instead of its LRIC. In the absence of any robust LRAIC+ / LRIC data, ComReg will use the standalone price of that unregulated service in the test on the basis that the standalone price recovers the long-term cost of the product or any other proxy / benchmark for long-term cost that ComReg considers is appropriate.

Possible further specification of the obligation not to cause a margin/price squeeze in WBA:
It is proposed that if a Bundle that includes WBA does not pass the Margin Squeeze Test, ComReg will carry out a general assessment of the Bundle and may conclude that, notwithstanding the fact that the Bundle fails the Margin Squeeze Test, the offer for sale by Eircom of that Bundle does not constitute a breach of the obligation under ComReg Decision D06/11 not to cause a margin/price squeeze. For the purposes of such assessment, ComReg may, in particular, have regard to any robust evidence of retail efficiencies or increased customer lifetimes resulting from the relevant Bundle. ComReg also proposes to consider the impact of the Bundle on competition, including by reference to the promotion of sustainable competition in the medium to long term and the likelihood of any potential foreclosure and associated consumer harm.

ComReg seeks views as to whether the existing obligation not to margin/price squeeze in WBA should be further specified to include passing a margin squeeze test for bundles that include WBA. Such a possible margin squeeze test would be similar to the proposed revised net revenue test in the Retail Fixed Narrowband Access markets as set out in Chapter 6, complemented by an assessment of the competitive context. In particular, this proposed test in WBA would deal with bundles including the wholesale equivalent of SAB/Naked DSL to ensure that OAOs availing of Naked WBA (Bitstream) DSL are not being squeezed at the retail level.

Q. 8. Do you believe that the existing obligation not to margin/price squeeze in WBA should be further specified to include passing a margin squeeze test for bundles that include WBA? Do you agree or disagree that such a margin squeeze test should be similar to the proposed revised net revenue test in the Retail Fixed Narrowband Access markets? Please explain your response.

9.12 In relation to notification and compliance with the possible further specification set out above, ComReg is of the view that existing requirements under D06/11 and D01/06 would continue to apply.

Should D01/06 be amended from SEO to EEO?

9.13 ComReg could potentially provide Eircom with further pricing flexibility at some future stage, should the market conditions warrant such an adjustment, by allowing the retail costs associated with the provision of broadband to be determined on the basis of EEO (rather than SEO). Such a change would require amendment to D01/06 and notification to the European Commission. In the context of moving to a cost-based maximum price control for WBA, as noted in Consultation Document No. 10/56, any associated retail to wholesale margin squeeze test is likely to be based on EEO / competition law principles. ComReg plans to issue a consultation in relation to a cost-based maximum price control for WBA in early 2012. It follows therefore that, subject to the outcome of that consultation, the D01/06 SEO retail-minus price control could potentially be replaced approximately a year from now.

9.14 EEO means using Eircom's costs without any adjustments for scale. SEO means using Eircom's costs with an adjustment for economies of scale and scope. Economies of scale mean that the SEO has a lower volume than Eircom and as a result of this lower volume implies that its unit costs will be higher. Economies of scope mean that the SEO has a smaller number of products than Eircom over which to spread its overhead costs. Consequently, for the same total cost, an EEO would have a lower per unit cost than a SEO as an EEO has a larger scale and product scope.

9.15 The idea of a SEO recognises that in a regulated market where competition is being introduced it would be difficult, if not impossible, for an entrant at the time of entry to be as efficient as the incumbent.

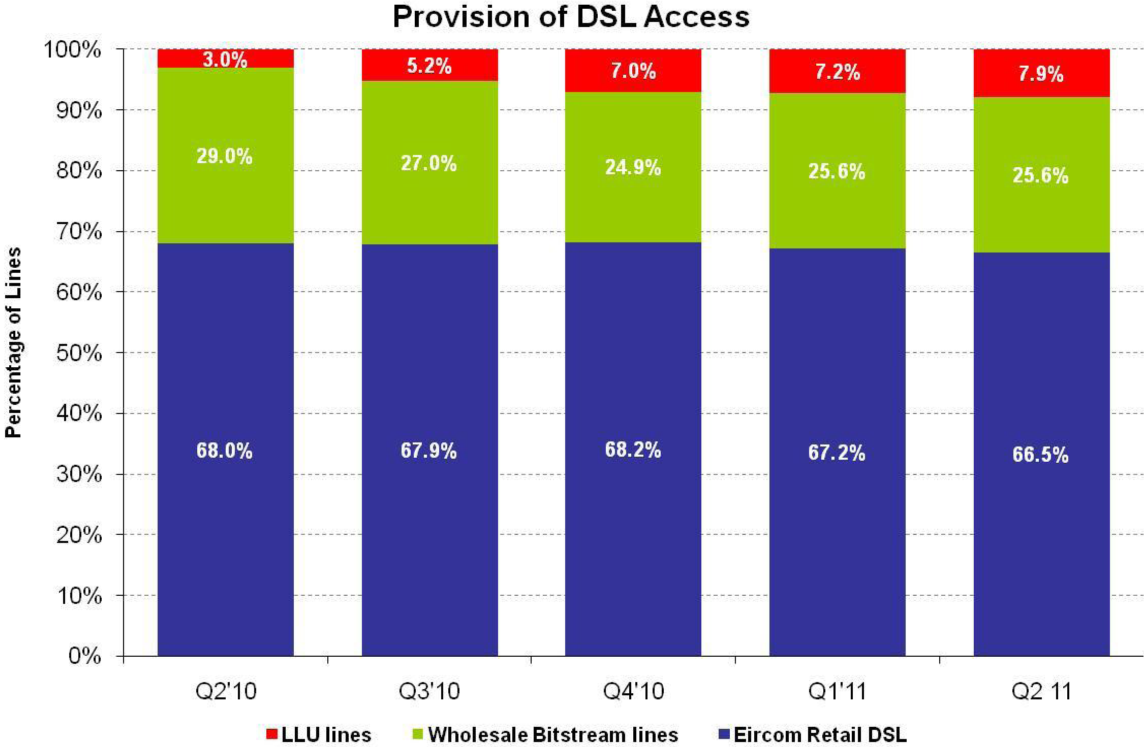
9.16 However, ComReg recognises that there may be a valid argument that any decision to continue with SEO should consider whether a move to EEO is possible over the medium to long-term — otherwise it could be argued that there is a risk of permanently supporting less efficient entry which results in higher wholesale prices which lead to higher retail prices to the detriment of consumers. The D01/06 retail-minus price control based on SEO has been in existence since 2006 and competition, for the most part, is no longer entry based but based on churn of existing customers.

9.17 Therefore, ComReg recognises that the retail-minus price control for WBA which is based on an SEO could warrant amendment to one based on an EEO in the future if market conditions were to warrant such a change.

9.18 However, ComReg believes that caution should be exercised before it is decided to use EEO instead of SEO — as the SEO standard recognises that entrants do not benefit from the same level of scale and scope economies as Eircom and therefore the entrants' unit costs are higher than those of Eircom.

9.19 Looking at the current market conditions, ComReg believes such an amendment may not be warranted at this time — as Eircom continues to hold a significant market share of DSL broadband lines as the latest Quarterly Report shows and, as noted in the recent WBA market review, Eircom is still a major provider of retail broadband. The D01/06 price control assumed the SEO would have a 25% market share.

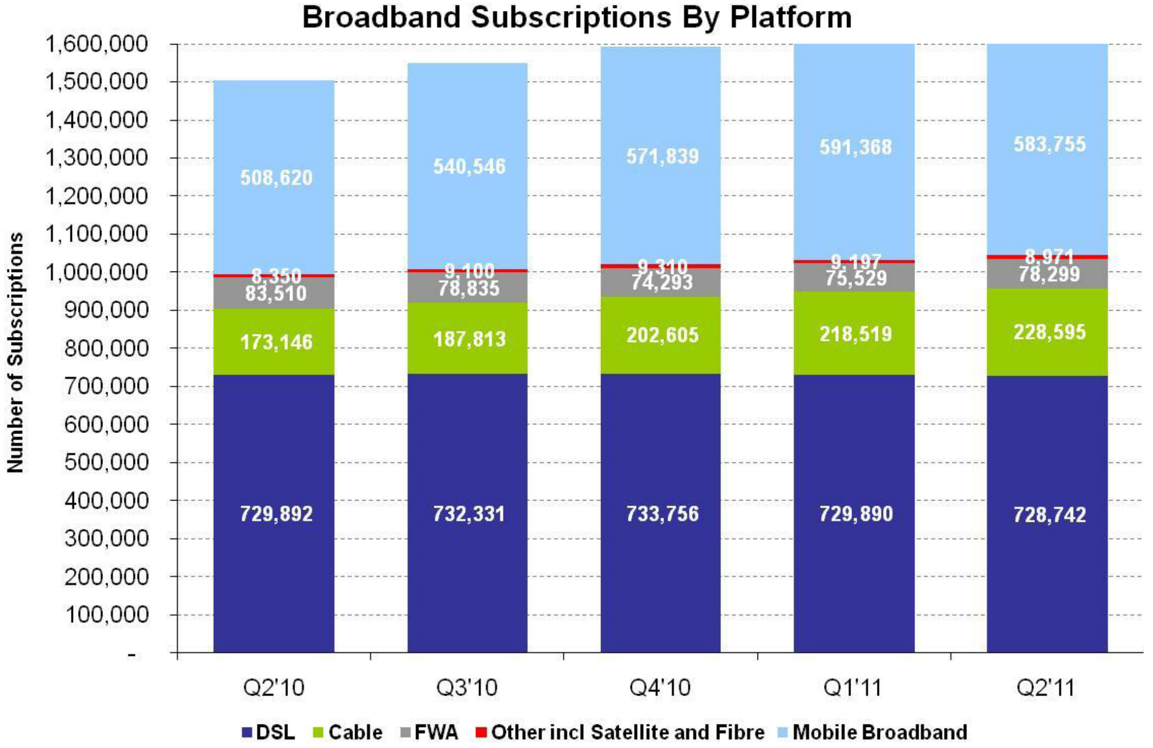
Figure 8: Provision of DSL access by Eircom retail DSL and OAO DSL (WBA and LLU)



Source: Quarterly Key Data Questionnaire

9.20 As can been seen from Figure 8 above, Eircom's market share of DSL broadband lines has not changed significantly over the years and has remained just below 70%. This is against the background of a recent uptake in LLU based competition and a possible trend of more localised competitive pressures from cable emerging in the retail market which can be seen in Figure 9 below. Figure 9, which is from ComReg's recent quarterly report for retail broadband subscriptions by platform (including platforms beyond DSL) shows that over the past year cable has increased its broadband subscriptions by just over 55,000 with DSL remaining unchanged:

Figure 9: Retail broadband subscriptions by platform



Source: Quarterly Key Data Questionnaire

9.21 ComReg believes that for Eircom to use EEO for retail broadband costs would require a further up-take of LLU or WBA inputs by OAOs relative to Eircom's share. ComReg believes that Eircom's recent wholesale reform announcements should ensure that OAOs are availing of wholesale products on a fully equivalent basis and without discrimination which should encourage OAOs to gain market share in 2012.

9.22 ComReg considers that it is reasonable to apply a REO / SEO standard in some markets and an EEO in other markets. There is nothing inconsistent in advocating one standard for some markets and another standard for other markets. Consequently, given the above observations, ComReg would welcome views as to whether, when and where it would be appropriate to use EEO to calculate Eircom's retail broadband costs in the net revenue test — as opposed to the current use of the SEO costs calculated by the retail-minus D01/06 price control in the market of WBA. In any event, subject to respondents' views and other relevant evidence by separate consultation, it is currently the intention of ComReg over the next twelve months to propose the replacement of D01/06 with a cost based price control. Therefore, the retail minus regime may potentially no longer be required which would have an impact on the likely margins allowed to OAOs for retail broadband.

Q. 9. Do you believe that the D01/06 price control should be amended from SEO to EEO? Please support your view with relevant data and evidence. If you believe it should remain at SEO, when do you believe it might be appropriate to use EEO? Please support your view with relevant data and evidence.

10 Naked WBA (Bitstream) DSL – obligation not to margin/price squeeze WBA and WPNIA

10.1 Recent regulatory forums have indicated a demand by OAOs for Naked WBA DSL. As technology develops, ComReg recognises that bundles that do not include retail fixed narrowband access, for example a bundle of "Naked" retail broadband and IP voice utilising that retail broadband, may become popular. As such bundles would not include retail fixed narrowband access, the net revenue test under Decision D07/61 would not apply. Therefore, ComReg is aware that such bundles could have a major impact and therefore appropriate ex-ante mechanisms need to be put in place to ensure competition to the benefit of end-users is maintained and encouraged.

10.2 However, ComReg is also cognisant that an offer of Naked DSL and its wholesale variant, Naked WBA (Bitstream) DSL, could be good for the market, allowing both Eircom and OAOs to offer bundles to consumers that do not include the full cost of PSTN line rental. It may also be the case that many consumers do not require or want a traditional phone line and just want fast, reliable standalone broadband. The regulatory framework needs to consider this; otherwise further regulatory uncertainty will arise in the coming years where SMP services are key inputs to these retail bundles.

10.3 At the outset and for the avoidance of any doubt, it should be clear that Eircom in offering Naked DSL to its retail customers and WBA equivalent to its wholesale customers must recover the efficient cost of its access network (i.e. it is subject to a cost orientation obligation for the costs of its access network). Currently, the wholesale charge to OAOs of the access network is €18.02 per month based on the national SB-WLR price which set on a retail minus basis against the retail line rental price of €25.36. Where Naked DSL does not include a line card, this line card cost may be removed where it is no longer necessary to the proper functioning of the line and therefore does not need to be recovered. To date no operator is selling Naked DSL/SAB and all line cards are still in place supporting PSTN voice for active lines. If Naked DSL/SAB is only available in particular areas of the country, it may be appropriate at that time to review the appropriate network cost for access to this service by using the BU-LRAIC Access model used for arriving at the current LLU price.

ComReg's main concerns

10.4 ComReg's main concerns are two-fold:

10.4.1 There should be no margin/price squeeze of Eircom's offer of Naked DSL/SAB services at the retail level to its wholesale equivalent, Naked WBA DSL. This was examined in Chapter 9 with views sought on a possible margin/price squeeze test in the WBA market.

10.4.2 There should be no margin/price squeeze of Eircom's offer of Naked WBA DSL to its other wholesale products, SB-WLR and ULMP. Without an appropriate price control, such an outcome would negatively impact the ladder of investment objectives set out by ComReg over the years and the relative incentives that may make an OAO build or buy wholesale services, including LLU. To date WLR and WBA have been key enablers of competition and consumer choice. Therefore, ComReg considers that inappropriate application of proposed changes to the margin squeeze test to be applied to Eircom could jeopardise this progress and lead to significant market exit of smaller players unable to offer Naked DSL/SAB under equivalent circumstances. This was examined in Chapter 8 with a proposed margin/price squeeze test in the WPNIA market to minimise the risk of Naked WBA DSL being priced too low relative to ULMP.

Naked WBA (Bitstream) DSL and existing obligation not to margin/price squeeze WBA

10.5 The following sets out a description of the existing obligation not to margin/price squeeze and its application to any wholesale offer of Naked WBA (Bitstream) DSL.

10.6 The existing D01/06 retail-minus price control includes an obligation not to margin (price) squeeze which is currently set on a SEO basis. ComReg confirms that this existing obligation not to margin (price) squeeze will apply to Eircom for any offer of Naked DSL against its wholesale equivalent, Naked WBA (Bitstream) DSL.

10.7 This will ensure that Eircom in making any offer of Naked DSL at the retail level does not squeeze the wholesale equivalent by reference to the SEO retail costs. This ensures that OAOs availing of Naked WBA (Bitstream) DSL can compete fairly in the provision of Naked DSL at the retail level.

10.8 Therefore, an offer by Eircom of Naked WBA (Bitstream) DSL whether standalone or bundled will be subject to the existing retail-minus price control in the WBA market under D01/06 which is set by reference to a SEO. As stated earlier, this price control will be subject to re-consultation in 2012.

Naked WBA (Bitstream) DSL and WPNIA

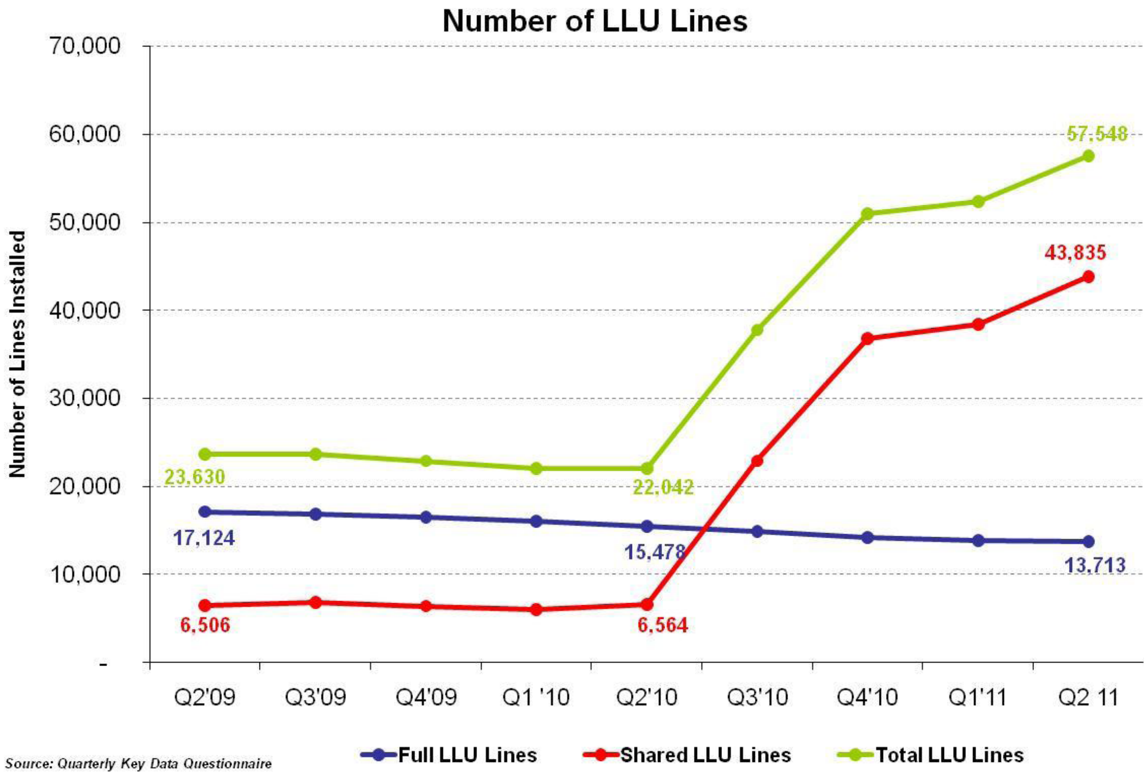
10.9 While ComReg acknowledges that there is a demand for Naked WBA DSL, it cannot allow Eircom to undercut resellers in areas where inter-platform competition is weak or non-existent as this would undermine any potential investment from other platforms in these areas — and would be contrary to ComReg's statutory and regulatory objectives.

10.10 WLR and WBA are and will continue to be important facilitators of competition in the retail narrowband and broadband markets. The inability of OAOs to replicate and effectively compete across these national markets could undermine competition and negatively impact on consumers in the long term where there is not an effective and transparent wholesale transition from the traditional voice services.

10.11 Without an appropriate specified price control, Eircom's pricing of Naked WBA (Bitstream) DSL might be set relatively too low and therefore might negatively impact investments in SB-WLR or WPNIA.

10.12 As can be seen in the charts below from the latest Quarterly Report, take-up of full LLU is still very low, especially when compared to the number of SB-WLR lines:

Figure 10: Number of LLU lines



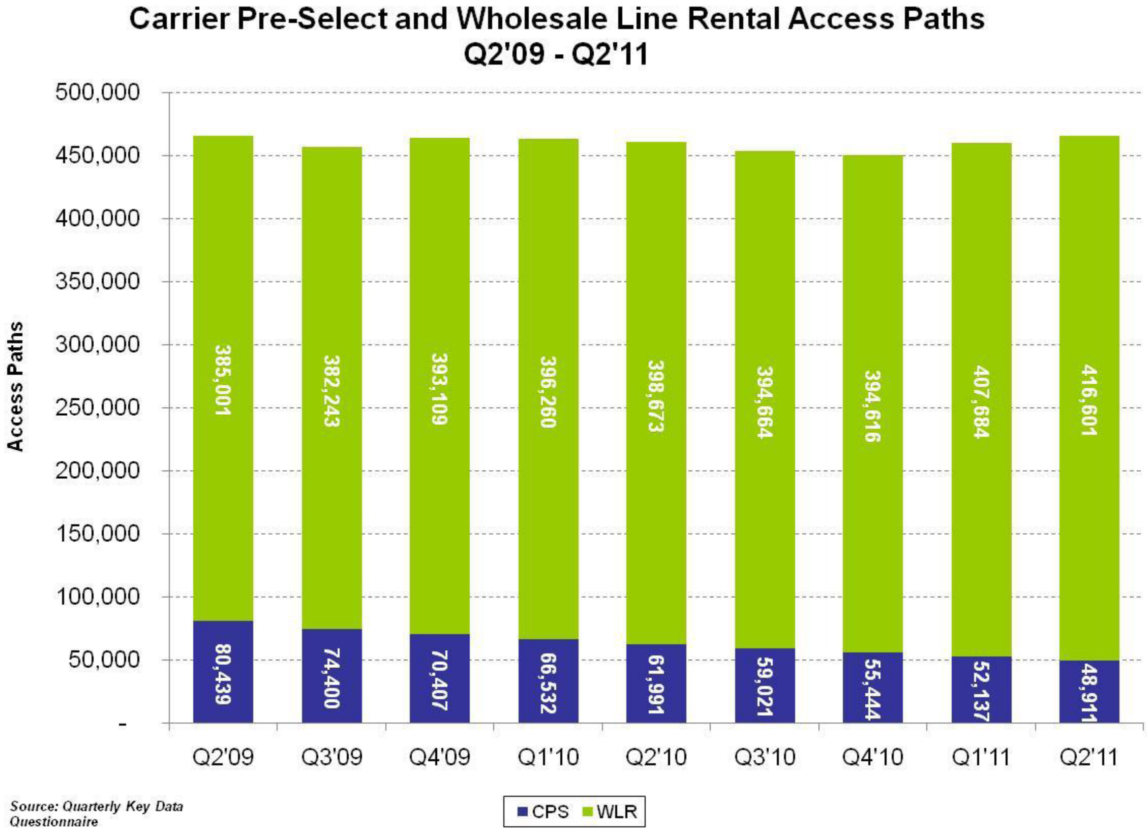


Figure 11: Number of WLR / CPS lines

10.13 Therefore, as set out in Chapter 8, ComReg proposes that the obligation not to margin/price squeeze WPNIA, which it is proposed to be further specified by a margin/price squeeze test for a REO, will apply to any offer by Eircom of Naked WBA DSL i.e. an appropriate economic space should be maintained between Eircom's pricing of its Naked WBA DSL product in the WBA market and its ULMP product in the WPNIA market.

10.14 However, Eircom is also subject to an obligation of cost-orientation in the WPNIA market to ensure that it recovers the efficient costs of its access network. In this respect and continuing the proposals of Chapter 8, assuming the current SB-WLR cost as being the appropriate WNI cost nationally, it is proposed that the national floor for Naked WBA (Bitstream) DSL could be as follows to ensure that there is no margin/price squeeze to WPNIA and to ensure that Eircom recovers its national costs of the access network. In the proposal below, ComReg has kept the cost of the line card or equivalent in the SB-WLR. ComReg seeks views if this line card is not used for voice provision, but is say used only for line testing, whether the cost of the line card or equivalent should be removed from the below:

If Naked WBA DSL is offered nationally:

WNI (incl line card or equivalent)	€18.02
DSLAM costs (based on DRAFT WBA minimum price floor model – subject to finalisation)	€6.88
Transport costs (based on DRAFT WBA minimum price floor model – subject to finalisation)	€3.75
Total National Minimum Price Floor for Naked WBA DSL to ensure no squeeze to ULMP (WPNIA)	**€28.65**

10.15 As set out in Chapter 8, if Naked WBA DSL is only offered in the same footprint of exchanges assumed to be unbundled when setting the maximum LLU price (i.e Areas 1 and 2 of Figure 4), it is proposed that the floor for Naked WBA (Bitstream) DSL could be as follows in order to ensure that there is no margin/price squeeze to WPNIA and to ensure that Eircom recovers its efficiently incurred access network costs in those areas:

If Naked WBA DSL is only offered in Area 1 and 2 of Figure 4:

WNI (in 149 exchanges as per LLU model)	€12.41
DSLAM costs (based on DRAFT WBA minimum price floor model – subject to finalisation)	€6.88
Transport costs (based on DRAFT WBA minimum price floor model – subject to finalisation)	€3.75
ULMP Fault Repair [149 exchanges] (€117.31*8%) / 12 [Actual fault repair cost * Fault % used in ULMP model]	€0.81
Line card (included in DSLAM cost above)	€0.00
ULMP connection and disconnection charges	€0.90
Total Minimum Price Floor for Naked WBA DSL in Areas 1 and 2 of Figure 4 to ensure no margin/price squeeze to ULMP (WPNIA)	**€24.75**

10.16 Furthermore, where Naked WBA DSL can only be offered in certain exchanges, due for example to technical restrictions, and where Eircom charge a lower price for ULMP in those exchanges, by reference to their own costs and / or the cost model used to set the maximum price for ULMP, ComReg is of the preliminary view that this lower price for ULMP could be used in the minimum price floor for that exchange as LLU based OAOs could avail of it also. Such an approach reflects ComReg's key concern of replication and non discriminatory behaviour. However, for the avoidance of doubt, it is for Eircom to ensure that it recovers its efficiently incurred costs in these exchanges where Eircom makes a commercial decision to offer its ULMP monthly rental below the maximum price set by ComReg.

Q. 10. Do you agree or disagree with ComReg's proposed floors for Naked WBA DSL to minimise the risk of a margin/price squeeze to WPNIA? Please explain your response.

11 Conclusion

Any relevant issues not considered in this consultation?

11.1 ComReg would also welcome any views respondents may have on relevant issues that ComReg has not considered in this consultation.

Q. 11. Are there any relevant issues that ComReg has not considered in this consultation? If so, please document and explain those issues fully and provide examples where appropriate.

Duration of this further specification

11.2 The further specifications outlined in the draft directions in this consultation will apply as long as Eircom is still found to have SMP in the relevant markets or until otherwise amended by ComReg.

12 Submitting Comments

12.1 All comments are welcome; however it would make the task of analysing responses easier if comments were referenced to the relevant question numbers and the numbered paragraphs from this document. Please also see ComReg Information Notice on ComReg Consultation Procedures (Document No. 11/34a) dated 6 May 2011.

12.2 The consultation period will run from 10 October 2011 to 21 November 2011 during which ComReg welcomes written comments on any of the issues raised in this paper.

12.3 Having analysed and considered the comments received and having taken utmost account of any comments by the European Commission, ComReg aims to publish a response to consultation and final directions in March 2012 which will, *inter alia* summarise the responses to the consultation.

12.4 In order to promote further openness and transparency ComReg will publish all respondents' submissions to this consultation and Consultation Document No. 10 / 01, subject to the provisions of ComReg's guidelines on the treatment of confidential information – ComReg Document No. 05 / 24[56].

Please note

12.5 ComReg appreciates that many of the issues raised in this paper may require respondents to provide confidential information if their comments are to be meaningful.

12.6 As it is ComReg's policy to make all responses available on its web-site and for inspection generally, respondents to consultations are requested to clearly identify confidential material and place confidential material in a separate annex to their response.

12.7 Such information will be treated subject to the provisions of ComReg's guidelines on the treatment of confidential information – ComReg Document No. 05 / 24.

[56] Guidelines on the treatment of confidential information - Final text of Guidelines

ANNEX A: Legal Basis

Retail Fixed Narrowband Access: Obligation not to unreasonably bundle

A1. By Decision D07/61[57], and pursuant to Regulations 25 and 26(4) of the 2003 Framework Regulations[58], ComReg designated Eircom as having significant market power ("SMP") on the markets for higher and lower level retail narrowband access from a fixed location (the "Retail Fixed Narrowband Access" markets). Under Sections 7.8 and 7.9 of the Decision Instrument annexed to Decision D07/61, and pursuant to Regulation 14 of the 2003 Universal Service Regulations[59], ComReg imposed an obligation on Eircom not to unreasonably bundle services.

A2. The issue of "unreasonable bundling" was discussed in paragraphs 6.216 to 6.234 of ComReg Document No. 07/26.[60] By way of example, paragraph 6.233 provided two specific instances of what can constitute "unreasonable bundling" for the purposes of Eircom's obligation under Decision D07/61 not to unreasonably bundle. In addition, paragraph 6.234 stated: "*The SMP operator must ensure that any bundle avoids a margin squeeze and passes a net revenue test*". ComReg Document No. 07/26 and Decision D07/61 are to be construed together for the purpose of Eircom's obligation not to unreasonably bundle. This is provided for in Section 1.1 of the Decision Instrument annexed to Decision D07/61, which provides *inter alia* as follows:

"*1.1 This Decision Instrument relates to the markets for higher and lower level retail narrowband access from a fixed location and is made by the Commission for Communications Regulation ("ComReg"):*

> …
>
> *v. Having had regard to the market definition, market analysis and reasoning set out in Document No. 07/26 and the reasoning and individual decisions set out therein and in the preceding parts of this Decision Notice and Decision Instrument, both of which shall where necessary, be construed with this Decision Instrument;…*"

A3. Regulation 14(1) of the 2003 Regulations (which has now been replaced by Regulation 13(1) of the 2011 Universal Service Regulations[61]) provided that where ComReg determined, as a result of a market analysis carried out in accordance with Regulation 27 of the 2003 Framework Regulations, that a given retail market was not effectively competitive and concluded that obligations imposed under the 2003

57 Decision D07/61 – Decision Notice and Decision Instrument - Designation of SMP and SMP Obligations - Market Analysis: Retail Fixed Narrowband Access Markets (24 August 2007).

58 European Communities (Electronic Communications Networks and Services) (Framework) Regulations 2003 (S.I. No. 307 of 2003), as amended (the "**2003 Framework Regulations**").

59 European Communities (Electronic Communications Networks and Services) (Universal Service and Users' Rights) Regulations 2003 (S.I. No. 308 of 2003), as amended (the "**2003 Universal Service Regulations**").

60 Response to Consultation and Consultation on Draft Decision: Retail Fixed Narrowband Access Markets (Document No. 07/26, 4 May 2007).

61 European Communities (Electronic Communications Networks and Services) (Universal Service and Users' Rights) Regulation 2011 (S.I. No. 337 of 2011) (the "**2011 Universal Service Regulations**").

Access Regulations[62] or Regulation 16 of the 2003 Universal Service Regulations would not result in the achievement of the objectives set out in section 12 of the Communications Regulation Act 2002, it could impose such obligations as it considered appropriate to achieve those objectives on an undertaking identified as having SMP on a given retail market.

A4. The obligation not to unreasonably bundle was imposed on Eircom in Decision D07/61 because ComReg considered that the obligations imposed on Eircom under the 2003 Access Regulations and under Regulation 16 of the 2003 Universal Service Regulations would not result in the achievement of the objectives set out in section 12 of the Communications Regulation Act of 2002. The imposition of the obligation not to unreasonably bundle was based on the nature of the problem identified in ComReg Document No. 07/26, was imposed pursuant to the market analysis in Decision D07/61 and was proportionate and justified in light of the objectives set out in section 12 of the Communications Regulation Act 2002.

A5. Regulation 14(2)(d) of the 2003 Universal Service Regulations provided the legal basis for the imposition under Decision D07/61 of the obligation not to unreasonably bundle. Regulation 14(2)(d) of the 2003 Universal Service Regulations has now been replaced by Regulation 13(2)(d) of the 2011 Universal Service Regulations. By virtue of the transitional provisions in Regulation 38 of the 2011 Universal Service Regulations, the obligation under Decision D07/61 not to unreasonably bundle is deemed to continue in force as if it was imposed under Regulation 13 of the 2011 Universal Service Regulations.

A6. Regulation 30 of the 2011 Universal Service Regulations states that ComReg may, for the purpose of further specifying requirements to be complied with relating to an obligation imposed by or under those Regulations, issue directions to an undertaking to do or refrain from doing anything which ComReg specifies in the direction. In this consultation, ComReg is proposing to issue such a direction to Eircom pursuant to Regulation 30, in conjunction with Regulation 13, of the 2011 Universal Service Regulations.

WPNIA: Obligation not to cause a margin/price squeeze

A7. By Decision D05/10[63], and pursuant to Regulations 25 to 27 of the 2003 Framework Regulations and Regulations 9 to 14 of the 2003 Access Regulations, ComReg designated Eircom as having SMP on the WPNIA market and imposed a number of SMP obligations. In particular, Section 12.4 of the Decision Instrument annexed to Decision D05/10 states that Eircom shall have an obligation not to cause a margin/price squeeze.

[62] European Communities (Electronic Communications Networks and Services) (Access) Regulations 2003 (S.I. No. 305 of 2003), as amended (the “**2003 Access Regulations**”).

[63] Response to Consultation and Decision - Market Review: Wholesale (Physical) Network Infrastructure Access (Market 4) (Decision No. D05/10, Document No. 10/39, 20 May 2010).

A8. The effect of the transitional provisions contained in Regulation 40 of the 2011 Framework Regulations[64] and Regulation 24 of the 2011 Access Regulations[65] is that Decision D05/10 is deemed to continue in force as if it was made pursuant to the 2011 Framework Regulations and the 2011 Access Regulations.

A9. Regulation 18 of the 2011 Access Regulations provides a legal basis for ComReg to issue a direction further specifying the obligation not to cause a margin/price squeeze set out in Section 12.4 of the Decision Instrument annexed to Decision D05/10.

Consultation requirements

A10. Regulation 12(3) of the 2011 Framework Regulations provides that, except in cases falling within Regulation 13(8) (i.e. exceptional cases involving urgency), before taking a measure which has a significant impact on a relevant market, ComReg must publish the text of the proposed measure, give the reasons for it, including information as to which of ComReg's statutory powers gives rise to the measure, and specify the period within which submissions relating to the proposal may be made by interested parties. Regulation 12(4) states that ComReg, having considered any representations received under Regulation 12(3), may take the measure with or without amendment. Regulation 12 implements Article 6 of the Framework Directive

A11. Regulation 13(3) of the 2011 Framework Regulations provides that, upon completion of the consultation provided for in Regulation 12, where ComReg intends to take a measure which falls within the scope of Regulation 26 or 27 of the Framework Regulations, or Regulation 6 or 8 of the Access Regulations, and which would affect trade between Member States, it shall make the draft measure accessible to the European Commission, BEREC and the NRAs in other Member States at the same time, together with the reasoning on which the measure is based. Regulation 13 implements Article 7 of the Framework Directive.

[64] European Communities (Electronic Communications Networks and Services) (Framework) Regulations 2011 (S.I. No. 333 of 2011) (the "**2011 Framework Regulations**").

[65] European Communities (Electronic Communications Networks and Services) (Access) Regulations 2011 (S.I. No. 334 of 2011) (the "**2011 Access Regulations**").

ANNEX B: Draft Directions

ComReg would appreciate respondents' views on these draft directions.

Q. 12. Do you believe that the draft text of the proposed directions are from a legal, technical and practical perspective, sufficiently detailed, clear and precise with regards to the specifics proposed? Please explain your response and provide details of any specific amendments you believe are required.

DRAFT DIRECTION IN RELATION TO DECISION D07/61

1. STATUTORY AND LEGAL POWERS

1.1 This Direction relates to a further specification of the obligation under ComReg Decision D07/61 not to unreasonably bundle services and is made by the Commission for Communications Regulation ("ComReg"):

(i) Pursuant to Regulations 13, 30 and 38 of the Universal Service Regulations;

(ii) Pursuant to and having regard to the Significant Market Power ("SMP") designation on Eircom Limited in the markets for higher and lower level retail narrowband access from a fixed location contained in ComReg Decision D07/61;

(iii) Pursuant to and having regard to the obligation imposed on Eircom Limited by Sections 7.8 and 7.9 of the Decision Instrument annexed to ComReg Decision D07/61 not to unreasonably bundle services;

(iv) Pursuant to and having regard to the functions and objectives of ComReg as set out in Sections 10 and 12 of the Communications Regulation Act 2002 (as amended) and in Regulation 16 of the Framework Regulations;

(v) Having, where appropriate, pursuant to section 13 of the Communications Regulation Act 2002 (as amended) complied with policy directions made by the Minister for Communications, Marine and Natural Resources;[66]

(vi) Having had regard to the analysis and reasoning set out in ComReg Document No. 07/26 and ComReg Decision D07/61, which shall both, where appropriate, be construed together with this Direction;

(vii) Having had regard to the analysis and reasoning set out in ComReg Document No. 10/01 and having taken account of submissions received from interested parties in relation to ComReg Document No. 10/01 following a public consultation pursuant to Regulation 19 of the European Communities

[66] Policy Directions made by Dermot Ahern TD, then Minister for Communications, Marine and Natural Resources, dated 21 February 2003 and 26 March 2004.

(Electronic Communications Networks and Services) (Framework) Regulations 2003;

(viii) Having had regard to the analysis and reasoning set out in ComReg Document No. 11/72 and having taken account of submissions received from interested parties in relation to ComReg Document No. 11/72 following a public consultation pursuant to Regulation 12 of the Framework Regulations;

(ix) Having notified the draft measure and the reasoning on which the measure is based to the European Commission, BEREC and the national regulatory authorities in other EU Member States pursuant to Regulation 13 of the Framework Regulations and having taken account of any comments made by these parties.

1.2 The provisions of ComReg Document No. 11/72, and the Response to Consultation and ComReg Document No. 11/72 shall, where appropriate, be construed together with this Direction.

2. DEFINITIONS

2.1 In this Direction, unless the context otherwise suggests:

"Average Total Cost (ATC)" means a cost standard which reflects all costs incurred in the provision of a product or service including variable, fixed, common and joint costs;

"Authorisation Regulations" means the European Communities (Electronic Communications Networks and Services) (Authorisation) Regulations 2011 (S.I. No. 335 of 2011), as may be amended from time to time;

"Bundle" means a package of services, consisting of Retail Fixed Narrowband Access and one or more other services, which is offered for sale by Eircom to end users;

"Framework Regulations" means the European Communities (Electronic Communications Networks and Services) (Framework) Regulations 2011 (S.I. No. 333 of 2011), as may be amended from time to time;

"Net Revenue Test" means the net revenue test set out in Section 4.3 of this Direction;

"Net Revenue Test Model" is the model approved by ComReg and used by Eircom to demonstrate whether a particular Bundle complies with the Net Revenue Test. Eircom will keep the model up to date and updates by Eircom are subject to ComReg approval;

"Other Authorised Operators (OAOs)" means operators other than Eircom who are deemed to be authorised undertakings under Regulation 4 of the Authorisation Regulations;

"Portfolio" means [*to be defined following consultation in line with discussion on pages 26 to 27 of ComReg Consultation Document No. 11/72*];

"Retail Fixed Narrowband Access" means higher and lower level retail narrowband access from a fixed location and shall be construed in accordance with ComReg Decision D07/61 (as may be amended from time to time);

"**Retail Fixed Narrowband Access Markets**" means the markets for higher and lower level retail narrowband access from a fixed location as defined in ComReg Decision D07/61;

"SB-WLR" means Single Billing Wholesale Line Rental;

"Total Monthly Adjusted Bundle Cost" shall be construed in accordance with Reference C8 at page 59 of ComReg Document No. 11/72;

"Total Monthly Bundle Revenue" shall be construed in accordance with Reference R4 at page 58 of ComReg Document No. 11/72;

"Total Monthly Portfolio Cost" shall be construed in accordance with Reference C9 at page 59 of ComReg Document No. 11/72;

"Total Monthly Portfolio Revenue" shall be construed in accordance with Reference R5 at page 58 of ComReg Document No. 11/72;

"**Universal Service Regulations**" means the European Communities (Electronic Communications Networks and Services) (Universal Service and Users' Rights) Regulations 2011 (S.I. No. 337 of 2011), as may be amended from time to time.

3. SCOPE AND APPLICATION

3.1 This Direction applies to Eircom Limited, its affiliates, subsidiaries, successors and assigns ("Eircom").

3.2 This Direction is binding upon Eircom and Eircom shall comply with it in all respects.

4. OBLIGATION NOT TO UNREASONABLY BUNDLE

4.1 Pursuant to Sections 7.8 and 7.9 of the Decision Instrument annexed to ComReg Decision D07/61, Eircom is subject to an obligation not to unreasonably bundle services. For the avoidance of doubt, this obligation includes that any Bundle offered by Eircom must avoid a margin squeeze and pass a net revenue test.

4.2 For the purpose of further specifying requirements to be complied with relating to Eircom's obligation not to unreasonably bundle services under ComReg Decision D07/61, and pursuant to Regulation 30 of the Universal Service Regulations, Eircom is hereby directed to comply with the Net Revenue Test as set out in this Direction.

4.3 In order to comply with the Net Revenue Test:

(i) as regards every Portfolio, the Total Monthly Portfolio Revenue shall be equal to or exceed the Total Monthly Portfolio Cost; and

(ii) as regards each individual Bundle, the Total Monthly Bundle Revenue shall be equal to or exceed the Total Monthly Adjusted Bundle Cost; and

(iii) when a given Bundle includes unregulated retail services, compliance with the Net Revenue Test (as regards such unregulated retail services) shall be evaluated in accordance with the basis of assessment outlined in the section headed 'Unregulated Retail Service Assessment' at page 60 of ComReg Document No. 11/72.

4.4 If a Bundle complies with the Net Revenue Test, as outlined in Section 4.3 above, it will be deemed to comply with the obligation under ComReg Decision D07/61 not to unreasonably bundle services. If a Bundle does not comply with the Net Revenue Test, as outlined in Section 4.3 above, ComReg will carry out a general assessment of the reasonableness of the Bundle and may conclude that, notwithstanding the fact that the Bundle fails the Net Revenue Test, the sale or offer for sale by Eircom of that Bundle does not constitute a breach of the obligation under ComReg Decision D07/61 not to unreasonably bundle services. For the purposes of such assessment, ComReg may, in particular, have regard to any robust evidence of retail efficiencies or increased customer lifetimes resulting from the relevant Bundle. ComReg will also consider the impact of the Bundle on competition in the Retail Fixed Narrowband Access Markets, including by reference to the promotion of sustainable competition in the medium to long term and the ability of entrants to enter that market.

4.5 For the purposes of the Net Revenue Test, Eircom shall reconcile, where possible, its ATC for the relevant Bundles to its audited separated (regulatory) accounts.[67]

Pre-launch assessment of Bundles

4.6 Prior to making a proposed new or revised Bundle available for sale to end users, Eircom shall furnish ComReg with a detailed written submission demonstrating that the proposed new or revised Bundle complies with the obligation under ComReg Decision D07/61 not to unreasonably bundle services and, in particular, with the Net Revenue Test set out in this Direction. The submission shall make full and true disclosure of all material facts for the purpose of demonstrating that the proposed new or revised Bundle complies with the obligation not to unreasonably bundle services and, in particular, with the Net Revenue Test set out in this Direction. In the submission, all assumptions should be clearly set out together with the rationale and supporting evidence for such assumptions and the likely effect if any such assumptions are not met. The Net Revenue Test Model presented should be capable of running scenarios for changed key assumptions. Any claims for retail efficiencies or increased customer lifetimes should be supported by robust evidence.

4.7 Upon receipt of the submission, ComReg shall review the submission and, within five working days, give or withhold approval for launch of the proposed new or revised Bundle. Such approval will not be unreasonably withheld. Eircom shall not launch any new or revised Bundle without having received such approval from ComReg. Prior to the expiry of the five working day period, ComReg may seek further information from Eircom to inform its decision as to whether approval to

[67] Eircom's current accounting separation and cost accounting obligations are set out in Response to Consultation Document No. 09/75 and Final Direction and Decision: Accounting Separation and Cost Accounting Review of Eircom Limited (Decision No. D08/10, Document No. 10/67, 31 August 2010).

launch should be given or withheld. If such further information is not provided by Eircom within ComReg's timeline or to the standard required by ComReg, approval shall be withheld pending the required information being made available to ComReg for review and consideration. Upon receipt of the requested information, ComReg will proceed to make a decision as to whether approval for launch of the new or revised Bundle should be granted or withheld.

Post-launch assessment of Bundles / assessment of existing Bundles

4.8 Once a new or revised Bundle is made available for sale to end users, Eircom must at all times ensure it meets its obligation under ComReg Decision D07/61 not to unreasonably bundle services and, in particular, that it complies with the Net Revenue Test set out in this Direction. Eircom shall notify ComReg immediately if it believes that any Bundle may not be so compliant.

4.9 If requested by ComReg, Eircom shall provide such data as may be required by ComReg to verify Eircom's ongoing compliance with the obligation under ComReg Decision D07/61 not to unreasonably bundle services and, in particular, Eircom's compliance with the Net Revenue Test as set out in this Direction. Eircom shall also provide any other relevant information required so that ComReg can make an informed decision as to whether Eircom is meeting its regulatory obligations including, in particular, its obligation not to unreasonably bundle services.

4.10 As regards the monitoring of ongoing compliance, if on the basis of its review of not less than two consecutive Net Revenue Test monthly data sets, complemented by its general assessment of the reasonableness of the Bundle (as provided for in Section 4.4 above), ComReg is of the view that the Bundle is non-compliant with the obligation under ComReg Decision D07/61 not to unreasonably bundle services, ComReg will inform Eircom in writing of such view. Upon receipt of such view, Eircom shall immediately refrain from selling or offering for sale the relevant Bundle to new customers and within twelve weeks withdraw the relevant Bundle from the market.

4.11 Alternatively, Eircom may submit to ComReg (at least one week prior to the expiry of the twelve-week deadline referred to in Section 4.10 above) a proposal to modify the relevant Bundle. In making such a proposal, Eircom shall be cognisant of any other regulatory notification requirements it may have, including its regulatory obligation to notify OAOs of any proposed change to the price of SB-WLR (as provided for under ComReg Decision D07/61). ComReg shall, prior to the expiry of the twelve week deadline, inform Eircom in writing of its view as to whether the proposed modified Bundle complies with the obligation under ComReg Decision D07/61 not to unreasonably bundle services.

4.12 ComReg's powers in respect of Bundles as set out in this Direction shall be without prejudice to its statutory enforcement powers provided for under, *inter alia*, the Communications Regulation Act 2002 (as amended) and the Universal Service Regulations.

5. MAINTENANCE OF OBLIGATIONS

5.1 If any section, clause or provision or portion thereof contained in this Direction is found to be invalid or prohibited by the Constitution, by any other law or judged by a court to be unlawful, void or unenforceable, that section, clause or provision or portion thereof shall, to the extent required, be severed from this Direction and rendered ineffective as far as possible without modifying the remaining section(s), clause(s) or provision(s) or portion thereof of this Direction, and shall not in any way affect the validity or enforcement of this Direction.

6. STATUTORY POWERS NOT AFFECTED

6.1 Nothing in this further specification shall operate to limit ComReg in the exercise and performance of its statutory powers or duties under any primary or secondary legislation (in force prior to or after the effective date of this Direction).

7. EFFECTIVE DATE

7.1 This Direction shall be effective from the date of its publication and notification to Eircom and shall remain in force until further notice by ComReg.

[...]
CHAIRPERSON
COMMISSION FOR COMMUNICATIONS REGULATION
THE [...] DAY OF [...] 2011

DRAFT DIRECTION IN RELATION TO DECISION D05/10

1. STATUTORY AND LEGAL POWERS

1.1. This Direction relates to a further specification of the obligation not to cause a margin/price squeeze, as set out in Section 12.4 of the Decision Instrument annexed to Decision D05/10, and is made by the Commission for Communications Regulation ("ComReg"):

(i) Pursuant to Regulations 13, 18 and 24 of the Access Regulations;

(ii) Pursuant to and having regard to the Significant Market Power ("SMP") designation on Eircom Limited in the market for wholesale physical network infrastructure access contained in ComReg Decision D05/10;

(iii) Pursuant to and having regard to the obligation imposed on Eircom Limited by Section 12.4 of the Decision Instrument annexed to ComReg Decision D05/10 not to cause a margin/price squeeze;

(iv) Pursuant to and having regard to the functions and objectives of ComReg as set out in Sections 10 and 12 of the Communications Regulation Act 2002 (as amended), in Regulation 6 of the Access Regulations and in Regulation 16 of the Framework Regulations;

(v) Having, where appropriate, pursuant to section 13 of the Communications Regulation Act 2002 (as amended) complied with policy directions made by the Minister for Communications, Marine and Natural Resources;[68]

(vi) Having had regard to the analysis and reasoning set out in ComReg Decision D05/10, which shall, where appropriate, be construed together with this Direction;

(vii) Having had regard to the reasoning set out in ComReg Document No. 11/72 and having taken account of submissions received from interested parties in relation to ComReg Document No. 11/72 following a public consultation pursuant to Regulation 12 of the Framework Regulations; and

(viii) Having notified the draft measure and the reasoning on which the measure is based to the European Commission, BEREC and the national regulatory authorities in other EU Member States pursuant to Regulation 13 of the Framework Regulations and having taken account of any comments made by these parties.

[68] Policy Directions made by Dermot Ahern TD, then Minister for Communications, Marine and Natural Resources, dated 21 February 2003 and 26 March 2004.

2. DEFINITIONS

2.1. In this Direction, unless the context otherwise suggests:

“Access Regulations” means the European Communities (Electronic Communications Networks and Services) (Access) Regulations 2011 (S.I. No. 334 of 2011), as may be amended from time to time;

“Downstream Regulated Wholesale Service” means a regulated wholesale service which is sold or offered for sale by Eircom to OAOs downstream from the WPNIA Market and contains a ULMP component (examples of such Downstream Regulated Wholesale Services include, for example, SB-WLR and Naked WBA (Bitstream) DSL);

“Framework Regulations” means the European Communities (Electronic Communications Networks and Services) (Framework) Regulations 2011 (S.I. No. 333 of 2011), as may be amended from time to time;

“Full Unbundled Access to the Local Loop” shall have the same meaning as in the Schedule to the Access Regulations, as may be amended from time to time;

“Local Loop” shall have the same meaning as under Regulation 2(2) of the Access Regulations, as may be amended from time to time;

“Margin/Price Squeeze Test” means the margin/price squeeze test set out in Section 4.2 of this Direction;

“Naked WBA (Bitstream) DSL” means any wholesale equivalent of Naked DSL;

“Naked DSL” means a digital subscriber line (“DSL”) without a Public Switched Telephone Network (“PSTN”) service, i.e. only a standalone DSL broadband service is provided on the Local Loop;

“Other Authorised Operators (OAOs)” means operators other than Eircom who are deemed to be authorised undertakings under Regulation 4 of the Authorisation Regulations;

“Reasonably Efficient Operator” means a reasonably efficient operator which has a different basic cost function to Eircom and does not yet enjoy the same economies of scale and scope as Eircom;

“SB-WLR” means Eircom’s Single Billing Wholesale Line Rental product;

“ULMP Price Control Model” means the model referred to in ComReg Decision D01/10 which is used by ComReg to calculate the maximum monthly rental price of ULMP;

“**Unbundled Local Metallic Path (ULMP)**” is the implementation of Full Unbundled Access to the Local Loop;

“**Wholesale Network Input (WNI)**” means the appropriate monthly cost of the ULMP component, as calculated by ComReg having regard to the ULMP Price Control Model;

“WPNIA Market” means the market for wholesale (physical) network infrastructure access (including shared or fully unbundled access) at a fixed location provided over Current Generation WPNIA and over Next Generation WPNIA; the term “WPNIA Market” shall be construed in accordance with ComReg Decision D05/10.

3. SCOPE AND APPLICATION

3.1. This Direction applies to Eircom Limited, its affiliates, subsidiaries, successors and assigns (“Eircom”).

3.2. This Direction is binding upon Eircom and Eircom shall comply with it in all respects.

4. OBLIGATION NOT TO CAUSE A MARGIN/PRICE SQUEEZE

4.1. Section 12.4 of the Decision Instrument annexed to ComReg Decision D05/10 imposed an obligation on Eircom not to cause a margin/price squeeze. For the purpose of further specifying requirements to be complied with relating to that obligation, and pursuant to Regulation 18 of the Access Regulations, Eircom is hereby directed to comply with the Margin/Price Squeeze Test (as set out in Section 4.2 below).

4.2. In order to comply with the Margin/Price Squeeze Test, the price at which Eircom sells or offers for sale a Downstream Regulated Wholesale Service must be greater than the sum of: (i) WNI and (ii) the unavoidable costs of a Reasonably Efficient Operator that must be incurred in order to provide a service equivalent to the relevant Downstream Regulated Wholesale Service.

5. MAINTENANCE OF OBLIGATIONS

5.1. If any section, clause or provision or portion thereof contained in this Direction is found to be invalid or prohibited by the Constitution, by any other law or judged by a court to be unlawful, void or unenforceable, that section, clause or provision or portion thereof shall, to the extent required, be severed from this Direction and rendered ineffective as far as possible without modifying the remaining section(s), clause(s) or provision(s) or portion thereof of this Direction, and shall not in any way affect the validity or enforcement of this Direction.

6. STATUTORY POWERS NOT AFFECTED

6.1. Nothing in this Direction shall operate to limit ComReg in the exercise and performance of its statutory powers or duties under any primary or secondary legislation (in force prior to or after the effective date of this Direction).

7. EFFECTIVE DATE

7.1. This Direction shall be effective from the date of its publication and notification to Eircom and shall remain in force until further notice by ComReg.

[...]
CHAIRPERSON
COMMISSION FOR COMMUNICATIONS REGULATION
THE [...] DAY OF [...] 2011

ANNEX C: DRAFT Regulatory Impact Assessment

C1. Regulatory Impact Assessment ('RIA') is an analysis of the likely effect of proposed new regulation or regulatory change. The RIA should help identify regulatory options, and should establish whether proposed regulation is likely to have the desired impact. The RIA is a structured approach to the development of policy, and analyses the impact of regulatory options on different stakeholders.

C2. ComReg's approach to the RIA is set out in the Guidelines published in August 2007 in ComReg Document Nos. 07/56 & 07/56a. In conducting the RIA, ComReg takes into account the RIA Guidelines[69], adopted under the Government's Better Regulation programme. Section 13(1) of the Communications Regulation Act 2002, as amended requires ComReg to comply with Ministerial directions issued. Policy Direction 6 of February 2003[70] requires that, before deciding to impose regulatory obligations on undertakings, ComReg shall conduct a RIA in accordance with European and International best practice and otherwise in accordance with measures that may be adopted under the Government's "Better Regulation" programme.

C3. In conducting the RIA, ComReg has regard to the RIA Guidelines, while recognising that regulation by way of issuing decisions, e.g. revising obligations or specifying requirements in addition to promulgating secondary legislation, may be different to regulation exclusively by way of enacting primary or secondary legislation. ComReg's ultimate aim in conducting a RIA is to ensure that all proposed measures are appropriate, proportionate and justified. To ensure that a RIA is proportionate and does not become overly burdensome, a common sense approach will be taken towards a RIA. As decisions are likely to vary in terms of their impact, if after initial investigation, a decision appears to have relatively low impact; ComReg may carry out a lighter RIA in respect of those decisions.

Steps Involved

C4. ComReg wishes to point out that since it is not imposing a new regulatory obligation on an undertaking, it is not mandatory for it to conduct a RIA. In relation to the current directions, ComReg has nonetheless decided to carry out a RIA in order to demonstrate that it has considered and evaluated the regulatory options available, with due regard to necessity, effectiveness, proportionality, transparency, accountability and consistency.

C5. In assessing the available regulatory options, ComReg's approach to RIA follows five steps as follows:
Step 1: describe the policy issue and identify the objectives
Step 2: identify and describe the regulatory options

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[69] See 'REVISED RIA GUIDELINES: How to conduct a Regulatory Impact Analysis' dated June 2009 @

http://www.betterregulation.ie/eng/Publications/Revised_RIA_Guidelines.pdf

[70] Ministerial Policy Direction made by the Minister of Communications, Marine and Natural Resources on 21 February 2003.

Step 3: determine the likely impacts on stakeholders
Step 4: determine the likely impacts on competition
Step 5: assess the likely impacts and choose the best option

Describe the policy issue and identify the objectives

C6. The first draft direction further specifies the obligation not to unreasonably bundle which currently pertains to the markets for higher and lower level retail narrowband access from a fixed location. As noted in the supporting consultations to ComReg Decision D07/61, while bundling can be welfare-enhancing for retail customers, it can also have negative consequences, in particular that the operator may use the retail prices of bundles to leverage its significant market power in retail fixed narrowband access into other retail markets – this is known as horizontal leverage. The regulatory objective of the obligation not to unreasonably bundle is to prevent or mitigate the possibility of anti-competitive behaviour such as horizontal leveraging from retail fixed narrowband access into other retail markets and/or to prevent the strengthening of entry barriers in the retail fixed narrowband access markets. Having considered all responses to Consultation Document No. 10 / 01 and cognisant of the time that has passed since that consultation; ComReg in this consultation is setting out its revised preliminary views and draft directions.

C7. The obligation not to unreasonably bundle includes that Eircom "*must ensure that any bundle avoids a margin squeeze and passes a net revenue test*."[71] The net revenue test mitigates the risk that Eircom sells retail fixed narrowband access below cost in a bundle. However, failure to pass the net revenue test does not automatically lead to a bundle being unreasonable. As a proportionate measure, ComReg considers any robust evidence of retail efficiencies or increased customer lifetimes as a result of bundling to assess against the loss of the bundle. ComReg also considers the likely impact on competition and the ability of entrants to enter/remain in the market and promote sustainable competition in the medium to long term. Therefore, it is possible for a bundle that fails the net revenue test and therefore does not cover its costs to be considered reasonable where there is substantive evidence to demonstrate no competitive harm may occur. In this consultation, ComReg has proposed a revised specification of the net revenue test.

C8. In this consultation and draft directions, ComReg has further specified the pre-notification and pre-clearance requirements of bundles that include retail fixed narrowband access to support the obligation not to unreasonably bundle. This is because significant issues can arise where bundles are launched which subsequently do not comply with the regulatory obligation not to unreasonably bundle. Significant consumer and competitive disruption can be caused by non-compliant bundles in the market which reinforces the need for robust *ex- ante* monitoring of bundles that include retail line rental prior to entering the market, therefore ComReg is further specifying the pre-notification and pre-clearance requirements of bundles that include retail fixed narrowband access.

[71] At para 6.234 of ComReg document No. 07/26 'Market Analysis: – Retail Fixed Narrowband Access Markets (Response to Consultation 06/39 and Consultation on Draft Decision)' dated 4 May 2007

C9. In relation to the second draft direction, this specifies that the existing obligation not to margin (price) squeeze in the market of Wholesale Physical Network Infrastructure Access ('WPNIA') will be based by reference to a Reasonably Efficient Operator ('REO').

C10. In proposing these directions, ComReg has been minded to the relevant objectives, as set out in section 12 of the Communications Regulation Act, 2002 as amended by the Communications Regulation (Amendment) Act 2007[72] ("the Act") to be taken into account when applying remedies which are as follows:

- Promote competition;
- Promote the interests of users within the community;
- Ensure that there is no distortion or restriction of competition;
- Encourage efficient investment in infrastructure; and
- Encourage access to the internet at a reasonable cost to end-users.

Identify and describe the regulatory options

C11. In relation to the first draft direction, as the existing obligation not to unreasonably bundle in the retail narrowband access markets already includes reference to the avoidance of a margin squeeze and the passing of a net revenue test, the available regulatory options in the current RIA relate to specifying any revision to the detail of that net revenue test and further specifying pre-notification, pre-clearance and modification / withdrawal obligations.

C12. In relation to the first draft direction, the possible specification options for the net revenue test, as an ex-ante imputation test include the following:

1. Should the test be removed (Retail Fixed Narrowband Access)?

2. Should the test be conducted on a product by product basis or on the aggregate of the products or a two-part approach, that is, on part 1 on the aggregate of the bundles and part 2 on individual bundles with a lower cost standard for retail costs associated with calls?

3. Should the test use the existing retail-minus price controls for stand-alone SB-WLR and WBA as the retail costs for these products in the test?

4. Should retail costs for retail calls be based on a cost standard lower than ATC for individual bundle assessment?

5. Should the Larger Exchange Area reflect Areas 1-2 of Figure 4 or Areas 1-3 of Figure 4?

5. Should the test in the Larger Exchange Area reflect a weighted average cost of the applicable wholesale input?

6. In the Larger Exchange Area, when should the tests consider an appropriate LLU+ as the wholesale input?

7. Should unregulated products and services bundled cover their LRIC subject to there being no cross-subsidisation. For mobile services, should the aggregate of the applicable unregulated product also cover its LRAIC+?

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8. Should bundles that include retail fixed narrowband access be notified and pre-cleared with ComReg?
9. How should unreasonable bundles be modified / withdrawn?

C13. In relation to the second draft direction, this specifies that the existing obligation not to margin (price) squeeze in the WPNIA market will be based by reference to a Reasonably Efficient Operator ('REO'). Options here could have included use of an Equally Efficient Operator ('EEO') but as the WPNIA market is at the early stages of development, the use of EEO would not be appropriate at this time as no operator has achieved the same economy of scale and scope as Eircom. ComReg believes a REO approach is reasonable as at this time no OAO has achieved the same economies of scale or scope as Eircom.

Determine the impacts on stakeholders and competition

C14. In assessing the impacts of the net revenue test for stakeholders and for competition, there are a number of reasons why the proposed revision to the net revenue test in Retail Fixed Narrowband Access would be considered consistent with ComReg's statutory objectives under Section 12 of the Act:

a. Promoting the interests of users within the community
Safeguarding efficient competitors from possible below cost selling by an SMP operator in respect of bundles that include retail fixed narrowband access helps to facilitate greater regulatory certainty for longer-term competitive entry and expansion, with positive implications for the price, choice and quality of services ultimately delivered to end-users.

b. Ensuring that there is no distortion or restriction of competition
By seeking to pre-empt the possibility for anti-competitive bundling practices by an SMP operator to induce strategic barriers to entry in markets, the net revenue test would thus ensure that competitors can enter and sustain competition in the markets for retail fixed narrowband access and in adjacent markets.

c. Encouraging efficient investment in infrastructure and promoting competition
The net revenue test, in taking account of the current state of competition in certain areas, should encourage entry initially and expansion by competitors wishing to invest in their own infrastructure over time. At the same time, the net revenue test should facilitate entry by competitors as efficient as the SMP operator which is consistent with encouraging efficient investment.

C15. In assessing the impacts of the proposed further specification of the current obligation not to margin squeeze in the WPNIA market, there are a number of reasons why the proposal would be considered consistent with ComReg's statutory objectives under Section 12 of the Act:

a. Promoting the interests of users within the community

Safeguarding efficient LLU based competitors from possible squeeze, either by an offer of Naked WBA or SB-WLR at too low a price, helps to facilitate greater regulatory certainty for longer-term competitive entry and expansion, with positive implications for the price, choice and quality of services ultimately delivered to end-users.

b. Ensuring that there is no distortion or restriction of competition

By seeking to pre-empt the possibility for anti-competitive practices by an SMP operator to induce strategic barriers for entry in the WPNIA market, the specified obligation not to margin (price) squeeze would thus ensure that competitors can enter and sustain competition in the WPNIA market and thus the promotion of infrastructure based competition at the retail level.

c. Encouraging efficient investment in infrastructure and promoting competition

Protecting WPNIA from possible margin (price) squeeze by either Eircom's offer of Naked WBA or SB-WLR being priced too low, should ensure that entry and expansion by LLU based competitors wishing to invest in their own infrastructure over time is maintained.

Summary of Impacts on Stakeholders and on Competition

Option – That the net revenue test is removed		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Incumbent is subject to obligation not to margin/price squeeze under competition law. Withdrawal of net revenue test implies weaker mechanism for Eircom to demonstrate compliance with its regulatory obligations, namely that it is providing OAOs with effective and non-discriminatory wholesale access.	Competition law obligation is ex-post after any competitive harm may have occurred. Ex-post remedy under competition law may be too late for OAOs leading to exit.	Consumers may benefit initially from lower priced bundles from incumbent in certain areas. Where those low priced bundles are priced anti-competitively, consumers will lose over medium to long term due to potentially higher prices and reduced innovation following OAO exit.
Option – That the net revenue test remains unchanged		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
No additional impact on the incumbent, however, the current net revenue test may be limiting the incumbent to offer more	No additional impact on OAOs. The current net revenue test aims to ensure OAOs offering intra-platform competition are protected	Given the current structure of the net revenue test, consumers may not be getting lower priced bundles from the

competitive bundles, which ultimately should benefit consumers.	against possible horizontal leverage by the incumbent and that the SMP incumbent cannot sell retail fixed narrowband access below cost to the detriment of competition.	incumbent which could be feasible at this stage of market development while still promoting sustainable competition and choice over the medium to longer term.
Option – The Larger Exchange Area is defined as Area 1 – 2 of Figure 4		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Defining the Larger Exchange Area based on Area 1-2 of Figure 4 allows Eircom more pricing flexibility that if Area 1-3 was used as (1) there is a larger relative weighting of actual LLU take-up in Area 1-2 and (2) Area 3 has a higher network input cost than the maximum price of LLU.	Defining the Larger Exchange Area based on Area 1-2 of Figure 4 reflects OAOs unbundling to date and likely unbundling. OAOs to date have no visibility relating to possible virtual unbundling products as a result of NGA in Area 3.	Defining the Larger Exchange Area based on Area 1-2 of Figure 4 should allow Eircom to offer cheaper bundles to consumers in that area.
Option – That part one of the net revenue test is conducted on two portfolios (1) Bundles sold from within the Larger Exchange Area (2) Bundles sold from outside the Larger Exchange Area		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Allows the incumbent flexibility to price differentiate individual bundles within the aggregate of the bundles which ultimately should benefit consumers.	Allows the promotion of intra-platform competition by OAOs / entrants having a similar range of retail services and bundles as the incumbent. ComReg has set the aggregation of bundles reflective of the underlying structural conditions and the viability of unbundling. This approach should minimise the risk of inappropriate cross-subsidisation by the incumbent within the portfolios.	Provides ability to realise scope economies and cost savings in consumers' interests. Also allows the promotion of competition by OAOs / entrants which may have a smaller/different range of retail services and bundles as the incumbent to the benefit of consumers.
Option – That the net revenue test uses ATC as the appropriate measure of cost to assess the portfolio of bundles		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
ATC remains as the appropriate measure of cost in net revenue test, therefore no additional	Allows the promotion of competition by OAOs as ATC includes appropriate amounts of variable, fixed and common	Allows the promotion of sustainable competition by OAOs / entrants to the benefit of consumers in

impact on the incumbent. The use of ATC ensures that the incumbent recovers all its efficiently incurred costs and is therefore appropriate for the net revenue test.	costs, which is the calculus faced by any operator when deciding to enter or expand.	terms of price, choice and quality of services available over medium to longer term.
Option – That the net revenue test uses LRIC [which in this respect ComReg considers to be estimated by ATC less common costs and fixed indirect costs (akin to other common costs)] as the appropriate measure of retail cost for calls in individual bundles		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Allows flexibility to the incumbent to offer an individual bundle that does not recover common costs subject to the proviso that the aggregate of the similar bundles pass ATC.	OAOs who are as efficient as the incumbent and who offer similar bundles to the incumbent should be in a position to launch an individual bundle that does not recover common costs. OAOs have some comfort that Eircom's aggregate of bundles in a portfolio must cover its ATC thereby providing opportunity to recover common costs.	Allows the promotion of efficient competition to the benefit of consumers.
Option – That ATC, on a case-by-case basis, allows reflection of known future reductions in cost e.g. Mobile Termination Rates		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Allows the incumbent to reflect in its pricing known future changes in prices / costs which are supported by robust evidence which should ultimately be to the benefit of the consumer.	OAOs / entrants should also be able to factor known future changes in prices into their pricing decisions which will be to the benefit of end users. Eircom will be required to reconcile this ATC available from the audited regulatory accounts the following year. This should provide some assurance to OAOs that Eircom is covering its costs.	Allows pricing to reflect known future reductions in prices / costs which will be to the benefit of consumers now as opposed to waiting for the known cost reductions to come into effect.
Option – In area outside Larger Exchange Area, net revenue test remains based on SB-WLR / legacy WBA products		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
No additional impact on the incumbent as reflects	No additional impact on the OAOs as reflects current	No additional impact on customers as bundles

current approach for net revenue test.	approach for net revenue test and in those areas, SB-WLR and legacy WBA is predominant wholesale input used by OAOs.	currently offered to customers in these areas reflects this current approach and OAOs can offer competing bundles in those areas based on different WBA inputs provided by Eircom.
Option – That Eircom can use a weighted average of the actual wholesale inputs used by OAOs in the net revenue test in Larger Exchange Area		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
The approach reflecting actual use by OAOs of Eircom's wholesale inputs in the Larger Exchange Area allows Eircom to use a lower cost wholesale input in order to offer cheaper bundles to the benefit of end users. Encourages Eircom to promote the use of LLU by OAOs in order to further reduce the weighted average wholesale input.	Reflects the weighted average use of actual wholesale inputs by OAOs in the Larger Exchange Area. Those OAOs who remain on resale wholesale inputs only will find it harder to be competitive as LLU uptake grows. Approach should encourage OAOs to invest in infrastructure to avail of LLU inputs in order to be able to beat the weighted average input.	Customers should benefit from lower priced bundles and product innovation/differentiation in those areas where LLU competition is encouraged. OAOs that use Eircom's LLU product may be able to offer a more sustainable source of infrastructure-based competition in addition to any alternative platform competitors, e.g. Cable / WiMax which may further contribute potential competitive constraints to the benefit of consumers.
Option – Eircom can use LLU+/network input cost in the net revenue test in the Larger Exchange Area		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Allows Eircom to use lower priced LLU inputs offer cheaper bundles to the benefit of end users.	Not many OAOs currently on LLU based wholesale inputs – they will find it harder to be competitive and may be squeezed. This will either lead to exit or encourage investment in LLU in order to compete.	If OAOs cannot get a fit for purpose LLU product at certain exchanges, this option may result in their exit to the ultimate detriment of consumers. Eircom's customers may benefit from lower priced bundles initially but following market exit may be subject to increased prices and reduced service choice depending on strength of any residual competitive constraints from OAOs that continue

		to use Eircom's LLU product and/or alternative platform competitors e.g. Cable / WiMax
Option – That the net revenue test continues to use SEO for retail costs for broadband		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
No additional impact on incumbent as continuing existing position but it does not allow Eircom to possibly pass its lower retail costs onto customers as cheaper bundles. However, with proposed move to a cost-based price control to set the maximum price for WBA, subject to consultation, this SEO test may no longer apply – this could be in place by one year from now.	No OAO is currently as efficient as Eircom or as efficient as the SEO which assumed 25% share of broadband market. Therefore, continued use of SEO promotes entry/expansion and protects existing competition. Also, if EEO was utilised instead of SEO at this time, intra-platform competition would likely be adversely affected with possible exit from the market over the medium to long term.	Customers benefit from continued competition from OAOs using wholesale inputs provided by Eircom. Customers may not benefit from lower priced bundles from Eircom which could have been achieved by virtue of its lower retail costs but will benefit from the ongoing promotion of competition from OAOs relying on Eircom's wholesale inputs which, as identified in the market analysis, is still an important source of competitive impetus at this stage of retail market development.
Option – Unregulated products and services that do not rely on retail fixed narrowband access / wholesale broadband access will be included at LRIC cost standard subject to there being no cross subsidisation with retail fixed narrowband access. Absent LRIC / LRAIC+ information, stand-alone price or other appropriate proxy for long-term cost is used. For mobile services, in aggregate it must cover its LRAIC+.		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Will enable incumbent to include unregulated products and services in bundles at a competitive price while minimising the risk of any leverage.	Should minimise the risk of horizontal leverage to the detriment of competition as Eircom cannot cross subsidise with retail fixed narrowband access and must recover the long-term costs associated with the unregulated product.	Enables flexibility for all products to be included in bundles to the benefit of consumers thus promoting product innovation while also protecting against possible anti-competitive practices which could negatively impact on service price, choice and quality.
Option – That bundles including retail fixed narrowband access must be pre-notified by Eircom to ComReg		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**

Eircom is currently subject to a pre-notification requirement. The pre-notification requirement is further specified; however ComReg believes that the information sought in that pre-notification is not increased from the information currently provided by Eircom. ComReg believes that the pre-notification timing of five working days is not onerous or burdensome on Eircom.	Will give OAOs legal certainty that there will be regulatory monitoring of bundles provided by the SMP operator that include retail fixed narrowband access prior to their launch.	Ensures a transparent regulatory environment which monitors bundles at risk of being anti-competitive and which may have long-term negative impacts for consumer choice.
Option – That bundles including retail fixed narrowband access must be pre-cleared by ComReg as further specified in this consultation		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Eircom is currently subject to a pre-clearance requirement. The pre-clearance requirement is a further specification. This pre-clearance should give Eircom and ComReg some comfort that bundles will not cause a margin squeeze before they are launched. This should minimise the likelihood of bundles needing to be withdrawn as they are causing a margin squeeze, however, this can still occur for example if actual usage of the "free" allowance within a bundle is much greater than the forecast usage.	Will give OAOs some comfort that bundles launched should not cause a margin/price squeeze as they should meet the net revenue test – this will be confirmed based on actual results provided to ComReg. Such reassurance may support further market entry/expansion. Should minimise the risk of OAOs being adversely affected by bundles that are launched causing a margin squeeze – however such risk is not eliminated completely.	Less risk (but risk is not eliminated) that a launched bundle is found to be unreasonable and therefore consumers must be moved off the non-compliant bundle. Enhanced OAO confidence may also translate into more competitive offers and greater service choice.
Option – For bundles causing a margin squeeze, Eircom must withdraw / modify such bundles within twelve weeks		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
This is a further specification. It is believed that twelve weeks is sufficient time for Eircom to withdraw / modify a	Gives assurance to OAOs that bundles causing a margin squeeze will be modified / withdrawn within a reasonable timeframe thereby limiting	Eircom in its correspondence to retail consumers will ensure that retail consumers are informed of their right to

bundle as it recognises that if a change to retail line rental / SB-WLR is required, given Eircom's regulatory obligations, this may require up to 8 weeks. Therefore, the proposed twelve week period is considered reasonable.	their potential anti-competitive impact. The requirement that Eircom cannot add new customers to the non-compliant bundle within this twelve week period offers some further comfort to OAOs that the anti-competitive impact is minimised.	terminate their agreement without penalty. By not allowing Eircom to add new / existing customers to a non-compliant bundle, customers will be protected from joining a bundle that will be modified / withdrawn within twelve weeks.
Option – For margin (price) squeeze in WPNIA, use REO		
Impact on incumbent	**Impact on OAOs**	**Impact on consumer**
Allows Eircom to minimise the risk of a margin (price) squeeze to WPNIA, contrary to its existing regulatory obligation.	Allows the promotion of competition by OAOs / entrants which have a different cost base as the incumbent and which do not yet enjoy the same economies of scale.	Allows the promotion of competition by OAOs / entrants which are reasonably efficient to the incumbent to the benefit of consumers.

Assess the impacts and choose the best option

C16. Having reviewed the options above, ComReg proposes that:

1. It is legitimate and appropriate to apply the net revenue test as a two-part approach, namely that it applies both to individual bundles and to the aggregation of bundles. ComReg believes this approach will allow Eircom flexibility to price bundles to the benefit of end-users. Furthermore, in setting the aggregation of bundles, ComReg will ensure that the portfolio is replicable by OAOs and that OAOs do not face a risk of leverage as OAOs do not have the advantage of Eircom's incumbent base. Therefore, ComReg proposes two portfolios reflecting the different structural characteristics: (1) Bundles sold from Larger Exchange Area (2) Bundles sold from outside the Larger Exchange Area.

2. ComReg will define the 'Larger Exchange Area' following consideration of respondents' views to this Consultation and other relevant evidence.

3. For the time being, it is legitimate and appropriate for ComReg to continue to use the existing retail-minus price controls for narrowband and broadband as the retail costs in the net revenue test as to do otherwise would result in a different treatment within bundles. Notwithstanding this, there is some flexibility in that ComReg recognises that there may be some potential for double-count of certain retail costs when narrowband and broadband are bundled together e.g. billing costs. In the future, it may be appropriate to allow Eircom use retail costs for broadband based on EEO as opposed to the current SEO costs calculated by the D01/06 retail-minus price control. However, ComReg does not believe that competition is sufficiently developed at this time to consider the use of EEO for the retail costs of broadband but will reconsider the issue when reviewing the maximum ceiling price control for WBA.

4. ATC as the appropriate basis of cost in an ex-ante context for the portfolio of bundles. ATC is the correct cost input for the net revenue test in light of ComReg's statutory objectives under Section 12 of the Act to promote competition and protect the interests of end-users. In the context of an ex-ante regulatory tool to be applied by ComReg, ATC is the appropriate ex-ante cost basis to adopt as it should enable a potential entrant to recover all its efficiently incurred costs. ATC requires an operator with SMP to price at levels that include appropriate amounts of variable, fixed and common costs, which is the calculus faced by any operator when deciding to enter or expand. ComReg believes that, under the present market conditions in Ireland, this cost measure is the most appropriate way to promote competition under regulation, and to avoid further deterioration in the already weak nature of competition in SMP markets. However, ComReg proposes to allow the pricing below ATC for retail costs for calls in an individual bundle (with common and fixed indirect costs excluded for retail calls) and on a case-by-case basis if supported by robust evidence of retail efficiencies as a result of bundling and that the bundle is not having a negative impact on competition and the ability of entrants to enter the market and promote sustainable competition in the medium to long term. Furthermore, ComReg is now proposing to allow ATC reflect known future reductions in costs (e.g. Mobile Termination Rates) where these can be supported. ComReg believes that this allowance will allow end-customers to benefit from future known reductions in costs now.

5. For outside the Larger Exchange Area, ComReg considers it legitimate and appropriate to propose that the applicable wholesale inputs in the net revenue test remains at SB-WLR and legacy WBA. For the Larger Exchange Area, ComReg considers it legitimate and appropriate to propose a weighted average wholesale input of the applicable wholesale inputs used by OAOs in the area is taken as this reflects the actual usage of different wholesale inputs by OAOs in that area. ComReg believes that otherwise consumers may not be in a position to avail of lower prices for high speed broadband in that area, in particular where this is as a result of high unit costs driven by the national average cost of the copper access network. Thus the proposed approach recognises the importance of facilitating the development of efficient competition and the delivery of relevant competitive benefits to consumers.

6. ComReg believes that LLU competition is not sufficiently developed at this time to consider the use of LLU+ as the applicable wholesale inputs in the net revenue test in certain areas.

7. In relation to unregulated products and services bundled with retail fixed narrowband access, ComReg's concern is leverage. Therefore, it is legitimate and appropriate for ComReg to ensure that there will be no cross subsidisation between regulated products and unregulated products and that these unregulated products/services, when bundled, must cover their LRIC subject to the proviso that the aggregate of the applicable unregulated products and services cover their own LRAIC+. On a case-by-case basis, where there is unlikely to be medium to long term harm on competition, ComReg will consider AAC. In the absence of any LRIC / LRAIC+ cost information, ComReg proposes the use of stand-alone price or any other appropriate proxy of long-term cost.

8. It is legitimate and appropriate for ComReg to set out the notification process for new bundles or amendments to existing bundles and the process for the modification / withdrawal of bundles that are found to be causing a margin squeeze. ComReg has to date and will continue to be practical with its approach to reviews to ensure Eircom Retail is not unduly held back from launching legitimate bundles by unnecessary regulatory delays.

9. ComReg believes that revising the net revenue test and further specifying the notification, pre-clearance and modification / withdrawal requirements for bundles that include retail fixed narrowband access, is for the reasons set out in this consultation justified and should foster OAO and entrant competition in the retail fixed narrowband access and adjacent markets. It is therefore consistent with ComReg's statutory objectives under section 12 of the Act. Furthermore, ComReg believes that specifying the margin (price) squeeze obligation in WPNIA by reference to a REO recognises that no operator in WPNIA has achieved the same economies of scale and scope as Eircom at this time.

C17. ComReg is of the view that the proposed further specifications meet the six principles of "Better Regulation" as follows:

i. ComReg has clearly outlined why it is **necessary** to make these directions. ComReg believes the current net revenue test requires some refinements to ensure that it remains appropriate and to ensure that it is ultimately to the benefit of end customers. The further specification of the pre-notification and pre-clearance of bundles that include retail fixed narrowband access is necessary as it should minimise the risk of unreasonable bundles being launched by the SMP operator. The direction in the WPNIA market will minimise the risk of margin (price) squeeze in that market and promote competition and entry into that market and thereby promote infrastructure based competition at the retail level.

ii. ComReg considers that it has been **effective** in addressing the potential for anti-competitive behaviour by virtue of Eircom's SMP position in the markets for retail fixed narrowband access, WBA and WPNIA and its integrated position in relevant associated retail markets and is providing clear guidance to help guard against such potential anti-competitive behaviour;

iii. ComReg considers that it has been **proportionate** in its review. ComReg believes the proposed further specifications are not overly burdensome or onerous on Eircom and are in part aimed at introducing greater pricing flexibility for Eircom where this is proportionate to the observed structural conditions and prospects for future competitive developments;

iv. Having considered possible regulatory options and impacts for all stakeholders, ComReg considers its approach offers complete **transparency** in reaching the view that the net revenue test should be revised and that the obligation not to cause a margin (price) squeeze in WPNIA is further specified;

v. ComReg considers that it has been **accountable** in its review and that it has provided all of the detail, reasoning and information necessary to demonstrate how it reached the view that the net revenue test should be revised and that the obligation not to cause a margin (price) squeeze in WPNIA should be further specified;

vi. ComReg considers that its reasoning is **consistent** with previous ComReg views and in particular those expressed in the supporting market analyses.

Q. 13. Do you have any views on this draft Regulatory Impact Assessment and is there other factors (if any) ComReg should consider in completing its Regulatory Impact Assessment? Please explain your response and provide details of any factors that should be considered by ComReg.

ANNEX D: Summary of Responses to Consultation Document No. 10 / 01

D1. Set out in this Annex are the questions that were asked in Consultation Document No. 10 / 01, together with a summary of the responses from industry. As over a year has passed since that consultation, ComReg is allowing respondents the opportunity to revise their views if they wish. Therefore, except for the section on notification, pre-clearance, modification and withdrawal of bundles where for the most part ComReg's preliminary views still hold, ComReg has not provided its position but has generally set out its revised preliminary views in this consultation.

Overview of responses to Consultation Document No. 10 / 01

D2. On 6 January 2010, ComReg published ComReg Document No. 10 / 01. Four responses were received to the consultation from the following:

- Eircom Limited ("Eircom");
- BT Communications Ireland Limited ("BT");
- Vodafone Ireland Limited ("Vodafone"); and
- Hutchison 3G Ireland Limited ("3 Ireland").

D3. The response of 3 Ireland was a short letter generally noting that 3 Ireland believes that with the current net revenue test, ComReg is proposing the correct ex-ante imputation test to assess whether a bundle that includes retail fixed narrowband access is reasonable pursuant to ComReg Decision D07 / 61. In particular, 3 Ireland believes that ComReg should continue to apply the obligation not to unreasonably bundle (including the net revenue test) to individual bundles and not to the aggregation of bundles.

D4. In the following section, ComReg summarises the key points of the non-confidential response received from Eircom, BT and Vodafone in relation to each of the questions raised in the Consultation Document No. 10 / 01.

What ex-ante imputation test do you think is appropriate?

D5. In Consultation Document No. 10 / 01, ComReg asked respondents the following:

Consultation No. 10 / 01 Question

Q. 1. To meet the regulatory objectives of the obligation not to unreasonably bundle, what ex-ante imputation test do you think is appropriate to assess whether a bundle that includes retail fixed narrowband access is reasonable pursuant to ComReg Decision D07 / 61? To support your view, please detail your response setting out why you believe the proposed ex-ante imputation test meets the regulatory objectives of the obligation not to unreasonably bundle, detail the components of the test including why such components are appropriate and include worked examples of the test and its components where appropriate.

Views of Respondents

D6. **Vodafone** and **BT** generally agree that it is appropriate for ComReg to continue to use the current net revenue test as an ex-ante imputation test to assess whether a bundle that includes retail fixed narrowband access is reasonable. Eircom did not agree.

D7. **Vodafone** believes it is appropriate for ComReg to continue to use the current net revenue test based on the 'resale' wholesale Eircom inputs and the average total cost of Eircom. Vodafone believes the current net revenue test has proved an effective methodology for identifying and remedying unreasonable bundling. Furthermore, Vodafone believes that as well as being proportionate in addressing the specific market failure, the current net revenue test has proved to be relatively straight-forward to implement and monitor. Vodafone further believes that the form of net revenue test implemented, i.e. one akin to an EEO test, is optimal given the current state of competition in the market and the availability of the relevant information. Vodafone believes that the relative small number of components included in the test and the availability of much of the relevant input data significantly aids transparency and allows OAOs to perform their own indicative assessments of the reasonableness of any Eircom bundles.

D8. **Vodafone** in its response then examines each individual component of the net revenue test and generally agrees with them.

D9. **BT** believes that the current ex-ante net revenue test remains appropriate but believes that more substantive accounting information is required in Eircom's separated accounts to provide confidence on Eircom's costs and allocation methodologies.

D10. **Eircom** fundamentally disagrees that the obligation not to unreasonably bundle can be used to justify an ex-ante margin squeeze test for bundles. In any event, Eircom believes that it would be unreasonable, disproportionate and discriminatory to handicap Eircom through the imposition of onerous price floor hurdles based on a vague objective of "ensuring entry". In actual fact, Eircom states that it faces substantial and growing competition in the provision of bundles from several formidable market players who are well-established in the Irish marketplace and have no less favourable access to finance than Eircom and can call upon international marketing resources and experience that Eircom cannot. Eircom states that at least one of its competitors relies on own-infrastructure, and others are increasingly relying on LLU-based services. Eircom believes that a highly restrictive ATC test, applied at the most granular level, will not promote competition and refer to the report of their expert, Professor Gabel, to support this position.

D11. **Eircom** also maintain that the "no unreasonable bundling" test, as an element of the Universal Service Regulation, has retail consumers as its focus and cannot sustain a program focused on protecting efficient competitors, as may be inferred from the preliminary views set forth in Consultation Document No. 10 / 01. For these and other reasons contained in Eircom's response and the accompanying paper of Professor Gabel, Eircom urges ComReg to take a fresh look at the net revenue test and the objectives that ComReg is aiming to achieve.

D12. **Eircom** proposes the following approach, which they believe combines a reasonable degree of flexibility with appropriate constraints. They agree with the test being an EEO test but Eircom believe that the applicable cost standard should be Average Avoidable Cost ('AAC'). Eircom proposes the following:

- That Eircom's own retail costs will reflect the minimum retail-minus values for broadband and line rental, net of any efficiencies that can reasonably be estimated on the basis of quantifiable data, proxys as applicable,
- That the prices of the wholesale inputs will be those charged by Eircom, and for the broadband component will reflect the price of the lowest cost stack (typically, LLU).
- Any margin contribution associated with the unregulated components of the bundle (apart from calls) will be considered based on reasonable evidence, including applicable proxys or relevant proxies.
- Proposed bundles will be notified to ComReg 10 days in advance of launch, accompanied by a certification by Eircom that the bundles meet the prescribed test. The business case underlying the certification must confirm that each individual bundle is reasonably projected to meet the Average Variable Cost ('AVC') standard.
- The bundles will be monitored for each four-week period during a 6-month term. If the suite of bundles in the aggregate covers AAC on average over the 6-month period and in the last three four-week periods, the bundles will be allowed to continue without adjustment.
- Thereafter, Eircom will to provide semi-annual reports to ComReg provided that the suite of bundles, in the aggregate, continues to cover AAC. However, if the suite of bundles, in the aggregate, falls below AAC in any given four-week period, Eircom will be required to notify ComReg, providing full details, within 10 days of the close of the relevant four-week period, and monthly reporting will be reinstated if required by ComReg.
- If the suite of bundles, in the aggregate, fails to meet the ex-ante imputation test proposed by Eircom, Eircom will work with ComReg to select the optimal solution (withdrawal of some or all of the bundles, or an agreed form of adjustment). Eircom will provide adequate notification to customers, including a clear explanation of their option to reject any new contract without penalty, and Eircom will make every effort to minimise customer disruption.

Comments on the preliminary views expressed in Consultation Document No. 10 / 01

D13. In Consultation Document No.10 / 01, ComReg asked respondents the following:

Consultation No. 10 / 01 Question

Q.2. Do you agree or disagree with the preliminary views expressed by ComReg in the above (namely in paragraphs 2.18, 3.2, 3.9, 3.13, 3.14, 3.19, 3.24, 3.28, 3.35, 3.39, 3.46, 3.49, 3.50, 3.51 - 3.53, 3.60, 3.67, 3.68, 3.69)? Do you have any views on the matters ComReg seeks further input on in the above (namely in paragraphs 2.19, 2.20, 3.7, 3.17, 3.21, 3.23, 3.27, 3.36, 3.45, 3.58, 3.61, 3.64)? Please give a detailed response with examples where appropriate to support your view.

Views of Respondents

D14. **BT** agrees with all the preliminary views expressed by ComReg. BT states that it believes that Eircom has an extraordinarily high level of market share and consequential strength of branding. BT maintains that Eircom enjoys economies of scale and scope and is not constrained by functional separation obligations that would require it to provide equivalence of inputs. Thus, BT believes that there is a real potential for Eircom to leverage these opportunities whether unknowingly or for anti-competitive reasons and appropriate ex-ante remedies must be put in place. BT agrees with ComReg's preliminary view that the alternative tests proposed by Eircom could preclude efficient entry and would result in reduced incentives for operators to enter the market or to further invest in the market.

D15. In relation to the preliminary views expressed by ComReg in Consultation Document No. 10 / 01, **Eircom** and **Vodafone** responded as follows:

Para. No.	**Subject**	**Eircom**	**Vodafone**
2.18	EEO remains appropriate to test the existence of specific behaviour of the SMP operator in relation to the obligation not to unreasonably bundle.	Eircom agrees that EEO is the correct standard. Eircom believes a REO test would be disproportionate because, as the ERG Report on the application of margin squeeze tests to bundles (paras. 4-55), it would require Eircom to price its bundles artificially high in order to support inefficient or marginal competitors in the marketplace.	Vodafone agrees that ComReg should be wary of inefficient entry and should design the net revenue test accordingly. However, Vodafone believes that the EEO test (although mainly based on Eircom's costs) must contain sufficient adjustment to take account of OAOs reduced scale opportunities. On this basis Vodafone could agree with ComReg's preliminary view on this point.
3.2	Current framework for the assessment of whether a bundle is unreasonable under ComReg Decision D07 / 61 by reference to the net revenue test remains appropriate.	Eircom believes that applying the net revenue test on a highly disaggregated basis, at the individual sub-bundle level, would be unjustified and would impede, not promote, effective competition.	Vodafone agrees with the framework as currently set out and believes it to be sufficiently flexible to cater for possible amendments on enhancements.
3.9	It is appropriate to continue to use the average monthly revenue from an	Eircom considers that the average monthly revenue from a bundle family should be used to compute	Vodafone agrees.

	individual bundle as the revenue total in the net revenue test.	the net revenue for that bundle family for that month. Eircom agrees with using the package revenue and revenue from out-of-bundle charges in the test. However, Eircom believes that a finding of “unreasonableness” cannot fairly be made on the basis of a cost-price assessment of the bundles’ performance during a given four-week period, particularly in cases where a new bundle of services or a prominent new feature (for example, free calls to selected mobiles) is being introduced.	
3.13	That it is logical that the full retail price of retail line rental is included in the test to determine if the retail line rental is being sold below cost within a retail bundle.	Eircom does not disagree, assuming line rental continues to be regulated at the retail level on a retail-minus basis. Where LLU is economically efficient, Eircom believes that LLU should be used as the relevant input for a bundle of voice and broadband. Otherwise, Eircom believes that WLR and Line Share, or WLR and WBA (Bitstream), may be appropriate. Where WLR is a relevant input, Eircom believes that the costs should be Eircom’s actual retail cost (or the cost of the EEO), plus the actual WLR price (which is currently set at Retail minus a minimum percentage). Eircom notes that to the extent that actual retail costs are less than the specified percentage, and / or the WLR price is less than the maximum permitted, the	Vodafone agrees.

		sum of these costs will always be less than the full retail price.	
3.14	The WBA (Bitstream) price in the wholesale market as determined by Eircom is the applicable wholesale input cost.	Eircom believes that the price of LLU should be used. For the retail elements, Eircom agrees that the retail-minus value should be utilised (based on the application of the retail minus price control model).	Vodafone agrees that the use of the WBA (Bitstream) monthly retail price is the appropriate input for broadband and the retail costs associated with its provision using the regulated retail-minus.
3.19	To use LLU as the applicable wholesale input(s), the penetration of LLU would need to be significantly higher.	Eircom does not agree. Eircom believes that ComReg should consider the very real and potent facilities-based and platform competition that Eircom is now facing in key areas from cable, LLU and wireless broadband operators. Eircom maintains that the lowest cost stack (typically LLU) should be used to price the wholesale inputs from the inception of the new bundling regime.	Vodafone believes that LLU should not form part of the wholesale inputs for the imputation test until there is a further review of the Fixed Retail Narrowband Access market. Vodafone notes that the bundling obligation under discussion is a remedy which arises from Eircom's SMP finding in this market and that LLU obligations arise from the SMP finding in a separate market. Vodafone also notes that if LLU reaches penetration levels where it is considered to be relevant in relation to bundling, it is also likely that to be at a level which warrants a review of Eircom's SMP designation in the Fixed Retail Narrowband Access market.
3.24	Other wholesale costs.	Eircom agrees that the applicable wholesale prices in effect should be used, except in cases where there are established dates for changes in these costs that are programmed to occur during the test	Vodafone agrees with the use of the actual price of the relevant inputs at the time of the test unless there is robust evidence in support of guaranteed future changes. Vodafone believes that

		period. Eircom considers that international call costs should be based on market rates. Eircom offers wholesale international connection rates to OAOs in competition with other wholesale international call providers. The rates offered by Eircom are published in the CISPL (Commercial Interconnection Services Price List). As the net revenue test is a test of replicability, Eircom considers that the rates as published in the CISPL should be used as an appropriate input for international call costs similar to the manner in which Mobile Termination Rates are used for mobile call costs.	the use of Eircom supplied 'typical' usage patterns require close scrutiny by ComReg. Vodafone notes that usage patterns are like to be quite dynamic in the early stages of a new bundle lifecycle and ComReg must take expected changes in these patterns into account. As more bundles are tested for reasonableness, Vodafone believes that ComReg should increase and enhance its knowledge and experience of the usage patterns.
3.28	Use of AVC as the appropriate cost measure.	For the reasons set forth in Professor Gabel's paper, Eircom believes there are strong economic and public policy reasons for the use of AVC / AAC as the appropriate cost measure in the net revenue test as applied to bundles.	Vodafone agrees with ComReg that the use of AVC would not be appropriate as it sets too low a cost threshold for the use of an ex-ante imputation test. Vodafone believes that should AVC be adopted, market distortions in relation to new entry would likely occur as well as serious profitability concerns for existing competitors to Eircom.
3.35	Use of AAC as the appropriate cost measure.	For the reasons set forth in Professor Gabel's paper, Eircom believes that there is a strong case for the use of AAC as the appropriate cost measure in the net revenue test as applied to bundles.	Vodafone agrees with ComReg that the use of AAC is inappropriate in the context of an ex-ante imputation test under current market conditions. In particular, Vodafone believes that

			the exclusion of a provision for non-avoidable fixed and common costs would seriously disadvantage new and existing OAOs who do not enjoy Eircom's scale and scope economies. Vodafone believes that the use of AAC will lead to pricing at such low levels that new entry is choked off and existing competitive constraints are compromised.
3.39	Use of LRAIC+ as the appropriate cost measure.	For the reasons set forth in Professor Gabel's paper, Eircom believes that there are much stronger economic and public policy rationales for the use of LRAIC+ as the cost standard than for ATC; however, the AAC standard is the appropriate cost standard taking into consideration all relevant factors.	Vodafone agrees with ComReg that the use of LRAIC+ is inappropriate in the context of an ex-ante imputation test under current conditions. In Vodafone's view, current market and entry conditions dictate the continuing use of Average Total Cost ('ATC'). Vodafone believes that an imputation test using ATC ensures prices at a level that continues to facilitate efficient entry and maintains a competitive constraint on Eircom under current market conditions.
3.46	Source of ATC data in test.	Eircom notes that it continues to believe that the appropriate cost standard for the net revenue test should be avoidable cost rather than ATC. Eircom states that it has on a number of occasions communicated to ComReg the impracticality of requiring audit opinions at a specific	Vodafone agrees that the latest set of Eircom's externally audited separated accounts should be used as the relevant data in the net revenue test. Where it is not possible to extract the relevant cost data at the level of disaggregation required, Vodafone believes that ComReg

		service level as suggested. Eircom notes that it is not aware of any peer jurisdiction facing this type of requirement. Furthermore, Eircom believes that the requirement to perform an independent regulatory review in the absence of such a disproportionate audit is totally unwarranted. Eircom considers this position to be predicated upon an inappropriate view that no comfort can be drawn from an audit opinion delivered at a higher level, based upon the common system which produces these service costs. In Eircom's opinion, this view is both fundamentally flawed and at odds with the approach adopted by other NRAs.	should undertake an independent regulatory review and assess accordingly.
3.49	Retail costs for voice access market should be ascertained by deducting the price of wholesale SB-WLR from the retail line rental cost. However, retail efficiencies, where supported by robust evidence, implying a possibly lower retail line rental cost are assessed at a later stage in the framework to the extent that they may be replicable by an equally efficient OAO.	Eircom agrees that retail efficiencies associated with bundled services should be taken into account in the analysis. However, Eircom believes that ComReg should accept as evidence of efficiencies (for which there is unlikely to be any historical data given that the product is being introduced onto the market) estimates of cost savings related to identifiable efficiencies, as well as reasonable proxies or proxys from comparable jurisdictions where similar bundles are on offer.	No response.
3.50	Retail costs for	Eircom agrees to the use	Vodafone agrees that

	broadband access market if there is a move to a 'cost-plus' price control for WBA (subject to consultation)	of the retail cost based on the current retail minus price control model which should be added to the relevant LLU cost stack or cost-based WBA (Bitstream) prices in force from time to time.	ComReg should continue to use retail costs provided by Eircom to ensure that there is no margin squeeze in the WBA market and that this should continue in the event of a move to cost-plus methodology.
3.51 – 3.53	Unregulated products and services not included in Eircom's separated accounts and proposed two stage test.	Provided that the test is applied using EEO / AAC at the level of the suite of bundles, Eircom does not object to the proposed 2-stage approach. However, in regard to the stage-2 assessment (where necessary), Eircom vigorously objects to what amounts to a proposal to regulate a whole range of services (mobile broadband, IPTV, etc.) that are fully competitive and have never been subject to price regulation in Ireland (or indeed anywhere in the world of which Eircom is aware). Instead, Eircom believes that ComReg should evaluate the competitive dynamics of the bundles in question, for example, by considering the overall value of the regulated components as a percentage of the overall bundle value, and taking into account Eircom's relative market share (and any competitive disadvantages that it faces) in respect of the unregulated components. If, following this competition assessment, further information is required, Eircom believes that ComReg should be	Vodafone agrees with ComReg that even where unregulated products and services form part of a bundle, the net revenue test holds true. Vodafone agrees that where unregulated products and services from part of a bundle and the standalone retail prices (zero margin) of such products are used as the relevant input into the net revenue test then if the test is subsequently passed, no further action is required by ComReg. Where the test is failed, then Vodafone believes that the onus is on Eircom to fully satisfy ComReg as to why a margin greater than zero should be allowed as part of the test. Vodafone agree with ComReg that where unregulated products and services are likely to be an element of all foreseeable bundles then it may be beneficial – though not mandatory- for Eircom to provide this information on a confidential basis to ComReg as part of its separated accounts

		prepared to accept reasonable proxies or proxys for the unregulated components in cases where reasonable, service-specific cost data are unavailable.	submission.
3.60	Average customer lifetimes.	From a marketing perspective, Eircom believes that all operators view the provision of bundles as a way of reducing customer churn. Eircom notes that whether this will in fact prove to be the case over the longer term or in each instance, and whether some operators may have advantages over others in specific circumstances will be difficult to predict, and may differ for existing users (switchers) and new users coming into the marketplace. Eircom believes that these issues will need to be examined in context, depending on the composition of the bundles being reviewed. For example, in a bundle where “free calls to mobiles” is a key selling point, Eircom believes that the largest mobile player in the market may have a substantial advantage in signing up and retaining new to market customers, and in attracting and retaining customers from Eircom. If an Eircom customer switches from stand alone services to an Eircom bundle, Eircom believes that customer is more likely than a non-bundle customer to switch to a rival’s bundles given	Vodafone believes that the computation of average customer lifetime forms an important element driving the net revenue test. Vodafone believes that claims by Eircom that bundling will increase average lifetimes – even if intuitively correct – must be rigorously tested by ComReg before being incorporated into the test. Furthermore, Vodafone believes that the only relevant average lifetimes that should be taken into account are those relating to existing bundle customers. By virtue of its position as the incumbent and former monopolist, Vodafone believes that Eircom enjoys a legacy customer base of which a significant proportion have demonstrated little propensity to churn. Vodafone believes that lifetime calculations for these customers should not be combined with bundle customers to give a longer average. Vodafone agrees with ComReg that there may not yet be sufficient historical data to support the contention of increasing average

		experience gained with the bundle approach. Once a customer switches from Eircom, Eircom believes that the new vendor will (if competition is allowed to work in the Irish marketplace) offer additional features or new bundles in order to retain customers. Given the substantial marketing resources and experience of Eircom's key competitors (actual and potential) in the provision of bundles, Eircom would not expect efficient OAOs to be at any disadvantage to Eircom in terms of customer lifetimes in respect of bundled services; if anything, Eircom believes that the opposite is likely to be the case.	lifetime and that the issue should be reviewed in the medium term.
3.67	Different test for response to competitor bundle?	Eircom's position has been that, at a minimum, the AAC test should be applied in cases where Eircom is responding to a bundle that is already provided by one or more competitors in the marketplace (and therefore demonstrably replicable). For the reasons set forth in Professor Gabel's paper, Eircom believes that ComReg's assessment of the likely impact of this approach on competition in the relevant markets is incorrect. However, Eircom believes that the issue is moot if, as proposed above, ComReg adopts a more reasonable cost standard (i.e., not ATC at the	Vodafone agrees that it would be inappropriate to use a different imputation test on the basis of an Eircom claim that a particular bundle was launched only as a response to a competitor offer. If such a claim was allowed and resulted in a more favourable revenue test from Eircom's perspective, Vodafone believes that the possibility of regulatory gaming would become unacceptably high. Vodafone notes that ComReg already refers to possible Eircom delays in order to allow a competitor to launch first thereby allowing for the

		individual bundle level) for assessing bundles as the general rule.	'competitor response delay'. Indeed, Vodafone states it is hard to envisage why Eircom would not claim that every bundle product was launched as a competitive response and why they would not incorporate at least some features into the bundle that would support the claim. Vodafone believes that it would then be extremely difficult for ComReg to judge whether the bundle was a 'competitive response' since any customer choosing the bundle may do so on the basis of any of the included features and not just the particular one included as a competitive response. In summary, Vodafone believes that allowing a move to an AAC based test or some other lighter variant has the potential to completely undermine the efficacy of this form of obligation.
3.68	Different test for promotions?	Eircom believes that the treatment of proposed promotions should be considered on a case-by-case basis.	Vodafone agrees that any discounts and promotions should be taken into consideration in the proposed imputation test and that the bundle should be reasonable at all times.
3.69	Obligation applies to individual bundles - 'product by product' basis.	For the reasons set forth in Professor Gabel's paper, Eircom believes that the application of the cost standard at the highly granular level of the individual bundle will not	Vodafone agrees that the obligation should apply to individual bundles and not Eircom bundles at an aggregate level. Vodafone believes that this approach precludes

		help promote competition and will not be in the interests of consumers. Eircom believes that neither Eircom nor OAOs would assess the viability of a bundled offering on the basis of the individual broadband speeds available in the suite. Therefore, Eircom believes such a measure is disproportionate. Eircom notes that if a price floor is imposed at the level of each bundle, the relevant cost standard should unquestionably be AAC (with AAC or LRAIC+ applicable at the aggregate level). Furthermore, Eircom believes that if a test is applied at the bundle level, it should logically correspond to the baseline voice products rather than individual broadband speeds.	the possibility that Eircom could cherry pick particularly competitive segments for excessive discounting while maintaining an aggregate level of compliance.

D16. In relation to the further views sought, **BT** provided no further views. **Eircom** and **Vodafone** responded as follows:

Para. No.	**Subject**	**Eircom**	**Vodafone**
2.19	Should test be REO?	Eircom agrees that EEO is the correct standard. Eircom believes a REO test would be disproportionate because, as the ERG Report on the application of margin squeeze tests to bundles (paras. 4-55), it would require Eircom to price its bundles artificially high in order to support inefficient or marginal competitors in the marketplace.	Vodafone agrees that EEO is the appropriate test once the relevant adjustment is made to the SMP supplied data to account for its greater scale and scope economies.
2.20	Any	Test should be EEO /	Vodafone does not propose

	alternative tests?	AAC. Eircom notes that the criteria to assess any alternative tests is missing two important criteria, namely: (1) Does the proposed test promote investment by Eircom? By other operators? (2) Does the proposed test promote the introduction by Eircom (and / or other operators) of innovative products and services for consumers?	any alternative test.
3.7	Is Eircom's WACC a sufficient return in the test for operators as efficient as Eircom?	Eircom believes that any view to the contrary would re-open the REO / EEO debate, which should be resolved in favour of EEO. Moreover, Eircom believes that ComReg should recognise that in some circumstances Eircom will require a degree of the flexibility to use a ROCE for bundled products that is below the weighted average. Eircom notes that new innovations are risky, and sometimes fail. However, Eircom believes that a firm will try to achieve its average WACC over its portfolio: some products will be above average and some below. Eircom believes that it would not be sensible to cease a product offering after launch just because its return was slightly below the average WACC.	Vodafone believes that Eircom's WACC would not be sufficient for OAOs to cover their cost of capital and it is therefore not appropriate for the test. Vodafone believes that Eircom's market share, longevity; turnover and other factors mean it can enjoy access to capital – even in constrained times – that would not be available to the majority of OAOs. Vodafone believes that this means the imputation test could be passed on all cost inputs but the use of Eircom's WACC would still mean that OAOs could not support a competing bundle due to their higher cost of capital. Vodafone believes a higher rate of return should be used in the test at a level which reflects this higher cost of capital to many OAOs.
3.17 & 3.21	LLU (or variant thereof) in the test	For the reasons discussed by Professor Gabel, Eircom believes that LLU should be used to price the wholesale inputs from the inception of the new	Vodafone believes that LLU should not form part of the wholesale inputs for the imputation test until there is a further review of the Fixed Retail Narrowband Access

		bundling regime. Eircom believes that using the WBA (Bitstream) price as the input cost is likely to create perverse incentives on the part of OAOs and Eircom alike. At a minimum, Eircom believes that ComReg should examine the types of access that Eircom's competitors in the provision of particular types of bundles	market. Vodafone notes that the bundling obligation under discussion is a remedy which arises from Eircom's SMP finding in this market and that LLU obligations arise from the SMP finding in a separate market. Vodafone also notes that if LLU reaches penetration levels where it is considered to be relevant in relation to bundling, it is also likely that to be at a level which warrants a review of Eircom's SMP designation in the Fixed Retail Narrowband Access market.
3.23	Competition from other platform providers	As discussed in Professor Gabel's paper, Eircom believes that it will be put at an immediate commercial and competitive disadvantage if an inflexible ATC test applicable at the most granular level is applied. Eircom maintains that, although a reasonable set of cost principles should be established ex-ante for the assessment of bundles, a reasonable and proportionate approach will require ComReg to examine the competitive dynamics of each particular type of bundled product as they are proposed. Eircom believes that a bundle containing calls / access / broadband will involve entirely different market dynamics than triple- or quadruple-play bundles.	Vodafone notes that ComReg's SMP designation on Eircom's in the market for Fixed Retail Narrowband Access took account of the competitive influence alternative infrastructure providers. Since bundling is a remedy applied of the basis of this SMP designation, Vodafone believes that any change or flexibility in that remedy should only be considered once an updated market review in undertaken and the SMP designation is amended or removed.
3.27	Cost information	Eircom believes that ComReg should use the	Vodafone believes that ComReg must be satisfied

	required for the test needs to be supported by fit for purpose separated accounts with a sufficient level of granularity and it may mean that separated accounts are presented to ComReg for markets that are no longer regulated	best available cost and revenue data for its regulated services. Eircom believes that in some cases, well documented but as yet unaudited cost data should be examined if it shows an important trend that should be taken into account when basing decisions on audited data (which typically will be two years out of date). Eircom notes that it will work with ComReg to establish procedures for maintaining adequate record for services that were once regulated but have been de-regulated. Eircom vigorously objects to any proposal that it must provide audited separated accounts for services that have never been regulated (mobile broadband, IPTV, etc.).	that all separated accounts presented are fit for purpose. Vodafone recognises that there is a particular issue concerning the provision of information for non-regulated products or markets. However, Vodafone believes that that the bundling remedy cannot be efficiently applied without access to the actual information for these unregulated markets or through the use of a reasonable proxy. Vodafone believes it would be preferable that ComReg and Eircom reach agreement on the provision of information at a level of detail fit for purpose for purpose. In the absence of agreement, Vodafone believes that any proxy used must not be favourable to Eircom compared to the result likely to arise if the information was supplied voluntarily.
3.36	Use of AAC	No response given, but overall response from Eircom supports the use of AAC.	Vodafone agrees with ComReg that the use of AAC is inappropriate in the context of an ex-ante imputation test under current market conditions. In particular, Vodafone believes that the exclusion of a provision for non-avoidable fixed and common costs would seriously disadvantage new and existing OAOs who do not enjoy Eircom's scale and scope economies. Vodafone believes that the use of AAC will lead to pricing at such low levels that new entry is choked off and existing competitive constraints are compromised.

3.45	Relationship between bundles and marketing spend and Subscriber Acquisition Costs (‘SACs’)	Eircom notes that it is possible that over the longer term, as more and more existing and new customers sign up for OAO and Eircom bundles, all operators’ SACs could increase on average. In the near to mid-term however, Eircom states that these costs are declining and will continue to fall. Eircom believes that this trend can be expected to affect Eircom and OAOs in much the same way. However, Eircom vigorously disagrees that Eircom’s bundle-regulated SACs would be materially different from those of its competitors.	No views were provided by Vodafone.
3.58	Retail efficiencies as a result of bundling	Eircom notes that the types of efficiencies will depend on each particular bundle. Eircom states that there is a wide range of potential efficiencies that could be generated by bundle services. Examples include: elimination of distributor commissions, reduction in the number of sales calls for individual components, billing and administrative efficiencies, customer care efficiencies. Eircom believes that many types of efficiencies that are documentable may not be precisely quantifiable. In such cases, Eircom believes that ComReg should consider reasonable, conservative estimates, proxies, or relevant proxys, as appropriate.	Vodafone’s view is that any retail efficiencies which might accrue from bundling (e.g. combining the costs of marketing and supporting single products versus bundles) are more than negated by the added complexity associated with bundling. Vodafone states that, by its nature, bundling requires a greater amount of information to be communicated to customers to convey the advantages in terms of value and service which attach to the bundle. Vodafone believes that care costs are also greater with bundled products as they attract more calls and of greater duration (due to the added billing and feature complexity) than standalone products.

3.61	Data on average customer lifetimes	CONFIDENTIAL	Vodafone notes that bundled products are now common place in the market and have become the standard offering for many fixed operators. Vodafone states that in a relatively short period of time, significant volumes of customers have availed of bundled offerings and any stickiness which may have been apparent relative to standalone products is now largely irrelevant as bundles have become the standard offering.
3.64	Competitive context assessment of bundles	Eircom notes that if ComReg adopts the EEO / AAC test proposed by Eircom, the need for undertaking a qualitative competition assessment should be reduced. However, in any such assessment, Eircom believes that it will be important for ComReg to take into account the actual competitive dynamics affecting each particular type of bundle based on a variety of relevant factors. Depending on the circumstances, for example, Eircom believes that these may include the key features demanded by customers, the relative importance of the SMP component that is the focus of margin squeeze concern (e.g., narrowband access in this consultation) in relation to those features and its corresponding value as part of the overall bundle, the presence of any network effects and	No response.

		their likely impact, the market position of Eircom's main competitors in any key components, the comparability of any similar bundles already provided by OAOs on the market, etc.	

Pre-notification and pre-clearance requirements

D17. In Consultation Document No. 10 / 01, ComReg asked respondents the following:

Consultation No. 10 / 01 Question

Q. 3. Do you agree or disagree with the pre-notification and pre-clearance requirements for bundles that include retail fixed narrowband access as set out in the section above? Please explain your response and provide detailed information to support your view.

Views of Respondents

D18. BT and Vodafone agreed. Eircom did not agree.

D19. **BT** agrees with the pre-notification and pre-clearance requirements for bundles that include retail fixed narrowband access as set out by ComReg. BT states that Eircom has and continues to hold an extraordinarily high market share and Consultation Document No. 10 / 01 is the result of Eircom having launched bundles without pre-notification and clearance. BT agrees that significant consumer and competitive disruption is caused by non-compliant bundles in the market which reinforces the need for robust ex-ante monitoring of bundles that include retail line rental prior to their launch into the market and therefore agrees that ComReg should further specify the pre-notification and pre-clearance requirements of bundles that include retail fixed narrowband access. BT believes that the market was damaged as a result of Eircom launching such bundles. BT believes that the damage to the competitive market continues beyond the period in which the non-compliant bundles were available. BT notes that for the non-compliant bundles that Eircom launched in October 2008, it took approximately a year for ComReg to resolve the complaint due to legal challenge from Eircom. BT believes that pre-notification and pre-clearance give an appropriate signal to operators that they can invest in services without risk of being undermined without warning by unreasonable bundles. Thus, BT believes it is a pro-competitive approach and to be welcomed.

D20. **Vodafone** agrees with the pre-notification and pre-clearance requirements for bundles. Vodafone believes it is imperative that ComReg is given the opportunity to evaluate the relevant data prior to a bundle launch in order to ensure no unreasonable bundling has taken place. Absent this requirement, Vodafone considers that it would possible for Eircom to launch bundles and tie in significant volumes of internal and external customers (on contracts of at least 12 months) before ComReg issued a direction to amend or withdraw the offer. Vodafone notes that these customers are effectively non-contestable for the contract period. Vodafone also believes that it is reasonable to assume that the volume of customers captured in this manner would be material as significant investment is required to develop, support and market bundle offers, therefore it is reasonable to assume that Eircom would not undertake the investment without the reasonable prospect of attracting significant numbers of new customers.

D21. Vodafone believes that notification alone is not sufficient. Vodafone believes that ComReg must also issue a clearance to launch following its analysis of the Eircom supplied data. Vodafone agree that ten days provides sufficient time for ComReg to complete its analysis once there is no further clarification or addition information required.

D22. **Eircom** believes that the proposal that Eircom be required to pre-notify and pre-clear bundles that include retail fixed narrowband access with ComReg is unfair and disproportionate. Eircom believes it is unreasonable to single out Eircom as the only operator (fixed, mobile or cable) to be required to obtain permission to compete in the market. Under ComReg's proposals, Eircom states that it would be required to continue the process of compiling extensive information and modelling scenarios. Eircom considers that this places an enormous burden on resources that would be better applied in bringing innovations to customers. Eircom notes that under the current process, Eircom submits information to ComReg in order to obtain prior approval. This is in the form of:

(a) A cover letter to ComReg outlining the proposed bundle and the method of calculating the margin

(b) Where appropriate, a 'Statement of Compliance with ComReg D01 / 06' when broadband is included in the bundle (in Word format)

(c) Margin forecasts for the proposed bundle. This includes explanations of the customer data used, the scenarios for customer behaviour and summary of models using each scenario (in Word format)

(d) Detailed workings using customer data, tariff data and modelling of scenarios (in Excel format)

(e) A draft of the amendment to the Telecommunications Scheme.

D23. Eircom considers that it provides all information that ComReg deems is necessary to enable it to decide whether the bundles may be launched. In the event that ComReg requires further information, Eircom states that it deals with these as quickly as possible.

D24. Eircom believes that ComReg should accept Eircom's cost justification unless there is a patent error or flaw in the analysis. Eircom states that the draft direction should make clear that projections are susceptible to unanticipated developments and, therefore, actual performance can sometimes differ.

D25. Eircom notes that if it plans to launch a new concept in bundles, it may be difficult to provide robust evidence for retail efficiencies and / or increased customer lifetimes in advance of the bundle being launched. Eircom notes that ComReg proposes to require such evidence to be reconciled to accounting statements, audited and independently verified. Eircom believes that forecasts for new offers cannot meet such standards, so in effect ComReg is proposing only to consider these factors long after a particular bundle is launched. Eircom notes that it conducts market and other research to the extent possible to support its assumptions.

D26. Under the ComReg proposal, Eircom believes that it is imperative that should ComReg decide not to approve a bundle that a clear explanation be given to Eircom as to the reason why not. Eircom believes it should then be allowed to make an amended submission or to make a new submission. If, within the ten working days period in which ComReg reviews the proposed bundle, ComReg does request further information and Eircom provides this promptly within the period, Eircom believes that this should not be permitted to cause any unreasonable delays in the approval process.

ComReg's Position subject to respondents' views and other relevant evidence

D27. Since all respondents but Eircom agree with ComReg's preliminary view, in the remainder of this section ComReg sets out its reasons why it disagrees with Eircom's position that the requirement to pre-notify to ComReg and get pre-clearance from ComReg for bundles that include retail fixed narrowband access is unfair and disproportionate.

D28. Eircom is the only operator with SMP in the retail fixed narrowband access market. Pursuant to ComReg Decision D07 / 61, Eircom has existing pre-notification obligations. Similarly, where a retail bundle includes broadband, Eircom has existing pre-notification obligations. ComReg does not believe that the further specification of this decision is overly onerous and burdensome relative to the existing obligations.

D29. ComReg believes that the further specification of a pre-clearance from ComReg is required to minimise the risk of non-compliant bundles that include retail fixed narrowband access entering the market. This is clear from the October 2008 bundles that were launched despite concerns raised by ComReg pre-launch in relation to the assumptions made by Eircom for the new concept of free calls to Meteor. ComReg believes that the market was damaged as a result of Eircom launching such bundles and due to the time period of over one year it took to remedy the non-compliant bundles due to a legal challenge from Eircom. ComReg does not believe that the pre-clearance is onerous on Eircom and reflects the current position following the reaching of a settlement agreement between ComReg and Eircom in relation to the non-compliant bundles.

D30. ComReg will not cause any unreasonable delays in the approval process and if ComReg does not pre-clear a bundle it will make clear to Eircom the reasoning behind the decision so that Eircom can make an amended / new submission. For all new concepts in bundles, ComReg will be reasonable in its approach but would note that, as was the case with the October 2008 bundles, there is possible greater risk of below cost selling as there is many assumptions and little actual data therefore the onus is on Eircom to ensure a conservative approach is taken in the early months of the bundle so that the risk of withdrawal / modification is minimised. If based on actual data, it is shown that Eircom's forecast assumptions were too conservative Eircom is free to reduce the price of the bundle, or any other action it thinks is appropriate, post launch once it is not below cost selling. In this respect, for new concepts in bundling, ComReg believes there may be merit for soft or trial launches of such bundles by Eircom so that actual data can be obtained for a wider and more heavily promoted bundle launch a few months later.

Modification / withdrawal of non-compliant bundles

D31. In Consultation Document No. 10 / 01, ComReg asked respondents the following:

Consultation No. 10 / 01 Question

Q.4. Do you agree or disagree that if ComReg is of the view that a bundle in the retail fixed narrowband access market is unreasonable that Eircom should modify / withdraw such bundle within ten weeks? Please explain your response and provide detailed information to support your view.

Views of Respondents

D32. BT and Vodafone agreed. Eircom did not agree.

D33. **BT** agrees that if ComReg is of the view that a bundle in the retail fixed narrowband access market is unreasonable that Eircom should modify / withdraw such bundle within ten weeks. BT considers that failure to have such an obligation on Eircom could result in unreasonable bundles being in place for significant lengths of time causing ongoing damage to the competitive market. BT believes that the approach is pro-competitive and is to be welcomed.

D34. **Vodafone** agrees that a withdrawal of unreasonable bundles should happen for customers already on the non-compliant bundle. However, Vodafone believes 10 weeks is excessive as a timeframe to remedy the breach. Indeed, Vodafone considers that unreasonable bundling by its nature is a cause of market harm and should be dealt with by means of an urgent direction and not by standard breach notification. Vodafone believes that ComReg should instruct Eircom not to add additional customers to the non-compliant bundle from the date of the direction in relation to the non-compliant bundle. Absent such a direction, Vodafone notes that Eircom could continue to add customers in substantial numbers for an additional 10 weeks. Vodafone considers that it is likely that the attraction of the bundle to these additional customers is the very reason why the bundle has been designated as unreasonable.

D35. Vodafone further believes that all customers on a bundle which has been designated as non-compliant must be made contestable with a reasonable period. Vodafone suggests that within a period of 1 month Eircom must notify all the relevant customers of their ability to move supplier without penalty if they so choose. Vodafone considers that Eircom must not be allowed to migrate these customers to a new or amended (compliant) tariff with such a notification being issued.

D36. **Eircom** assumes that ComReg interprets that a bundle is unreasonable if the margin becomes negative. Eircom notes that Consultation Document No.10 / 01 proposes that Eircom to "notify ComReg immediately if it believes that any such bundle may not be compliant". Eircom notes that it does not produce net margin calculations on a monthly basis but rather for periods of four weeks and that the data for each four-weekly report that Eircom produces becomes available within a week of the end of the four-week period. Eircom further notes that two to three days are then required to validate the data. Therefore, Eircom notes that it will be a minimum of ten days after the end of the four-week period before a report can be produced.

D37. Eircom considers that the draft Direction in Consultation Document No.10 / 01 is silent on how ComReg will assess the "unreasonableness" of bundles after launch. Eircom considers that the following are the key issues:

- Over what period of time should the bundle be assessed (Eircom believes a minimum of 6 months is required)?
- On what basis should the bundle be assessed (Eircom believes that the assessment should be based on average margins over the 6-month period, provided that the bundles are margin positive in each of the last three months)?
- When can a more streamlined review process be implemented (for example, semi-annual reporting if the bundles meet the 6-month test)?

D38. Eircom considers that the assessment of a bundle must be made over a time period that is sufficient to provide a true reflection of customer behaviour, including customer familiarisation with and reaction to the bundle features. Furthermore, Eircom notes there may be seasonal factors that influence the actual margin calculations when compared to the predicted margins. There may also be external factors, such as an aggressive response by a competitor or adverse economic circumstances that influence the behaviour of the bundles. Eircom believes that a minimum of 6 months is required for a proper assessment.

D39. Eircom notes there may be unusual or unpredictable circumstances that affect bundles which could not have been foreseen prior to launch and which should be considered when assessing the reasonableness of bundles after launch. Eircom notes that it launches bundles to meet customer demand and needs. These are based on customer research and data analysis, and are clearly designed to respond to observed customer behaviour and lifestyle choices. Eircom states that to withdraw bundles that are designed to meet specific customer needs would be harmful to Eircom's reputation and commercially damaging. Therefore, Eircom notes that it has every incentive to price in accordance with proportionate pricing parameters. If, however, the bundles do not perform according to plan, Eircom states that it will be left with little choice but to modify a bundle that is deemed to be unreasonable. However, Eircom considers that this will present difficulties and may be impossible to overcome within the strictures – especially the ten week limit – of the draft direction. The following table submitted by Eircom lists the notifications that are required with respect to the scenarios outlined by ComReg in Consultation Document No. 10 / 01.

Table illustrating the bundle modification scenarios and associated notification timelines

Scenarios	Notification to ComReg per Regulations	Notification to OAOs	Notification to ComReg re: Telecommunic ations Scheme	Regulation 17 (4) Notification to Retail End Users	Notification Time Required
(i) Reduce the stand-alone price of retail line rental and its associated wholesale price, single bill wholesale line rental ("SB-WLR");	Two Months (per ComReg D07/61)	Seven weeks (per ComReg D07/61)	(a) Line Rental & Calls bundle: 5 working days (per ComReg D07/61) (b) Line Rental, Calls & Broadband bundle 15 working days (per ComReg D01/06)		Two Months
(ii) Increase the headline package price of the bundle	15 working days (per ComReg D01/06)	15 working days (per ComReg D01/06)	15 working days (per ComReg D01/06)	One Month	15 Working Days plus One Month
(iii) Increase the prices of calls outside the bundle allowance	15 working days (per ComReg D01/06)	15 working days (per ComReg D01/06)	15 working days (per ComReg D01/06)	One Month	15 Working Days plus One Month
(iv) Modify the "free" allowance within the bundle	15 working days (per ComReg D01/06)	15 working days (per ComReg D01/06)	15 working days (per ComReg D01/06)	One Month	15 Working Days plus One Month
(v) Reduce the price of the wholesale inputs mindful of the need to maintain an appropriate economic space relative to the prices of local loop unbundling ("LLU") wholesale inputs such that no margin or price squeeze occurs	Bit-Stream price change: 15 working days (per ComReg D01/06)	Bit-Stream price change: 15 working days (per ComReg D01/06)	Bit-Stream price change: 15 working days (per ComReg D01/06)		15 Working Days plus One Month

- D07/61 applies for change to line rental prices
- D01/06 applies for changes to bit-stream prices

D40. Eircom notes that the first scenario demonstrates that in order to meet its obligations, Eircom would be left with no more than two weeks to propose a modification to a bundle and to obtain ComReg approval.

D41. In the cases of scenarios (ii), (iii) and (iv) in the above table, Eircom considers that there are various practical difficulties. In some circumstances, Eircom notes one month's advance notification must be given to end users under Regulation 17. Eircom believes that if time is limited, in order to comply with obligations, this would have to be sent to customers before ComReg is formally given the 15 working day notification by way of a compliance statement under D01 / 06. Eircom believes that this is not practical.

D42. In addition to the scenarios proposed in the consultation, Eircom notes that it may be open to Eircom to modify elements of the bundles. For example a free Voicemail Box or other unregulated services could be withdrawn to move the margin to being positive.

D43. Eircom also notes that ComReg uses different measures of time that may give rise to confusion, these are:

- Working Days (e.g. 15 working days' notification to ComReg per ComReg D01 / 06)
- Weeks (e.g. Seven weeks' notification to OAOs per ComReg D07 / 61 and Ten Weeks in this Consultation Document No. 10 / 01)
- Months (e.g. Two Months' notification to ComReg per ComReg D07 / 61)

D44. Eircom notes that Consultation Document No. 10 / 01 proposed to direct that "Eircom shall pre-clear any communication [with customers] ... with ComReg" in the event of withdrawal or modification. Eircom believes that such an obligation would remove from Eircom a basic commercial freedom and that there is no justification for such an intrusive measure to engage with its own customers. Eircom notes that under Regulation 17 of the Universal Service Regulations operators, including Eircom, must notify customers one month in advance of 'modification in the conditions of the contract' and to advise customers of 'their right to withdraw without penalty from such contract'. Eircom notes that the regulations do not currently state that customers must be advised that they may 'move to another operator' as ComReg proposed in Consultation Document No. 10 / 01. Eircom believes that this additional requirement is also entirely inappropriate. Eircom notes that when customers are advised of changes they may choose to withdraw without penalty from their Eircom contract for the affected bundle (as is their right under Regulation 17) and take up a new contract for a different bundle with Eircom, or move to another operator. Eircom believes that the marketplace will ensure that customers are well aware of their options, and it would be entirely unwarranted and disproportionate for ComReg to require Eircom to provide free advertising for other operators.

ComReg's Position subject to respondents' views and other relevant evidence

D45. Based on the views of respondents and on further consideration, ComReg remains of the view that Eircom must withdraw / modify a non-compliant bundle within a specified period of time.

D46. ComReg agrees with Vodafone's point that this Direction should be amended to include that Eircom cannot add additional customers to the non-compliant bundle from the date of the bundle is deemed by ComReg to be non-compliant.

D47. In relation to Eircom's point over what period ComReg will consider whether a bundle is unreasonable, ComReg will add to the decision to clarify that the basis of the review will be at least two consecutive data sets. This position is consistent with the current settlement agreement in relation to bundles that include retail fixed narrowband access. ComReg believes that a minimum period of 6 consecutive data sets as proposed by Eircom in its response to Consultation Document No.10 / 01 is too long if such a bundle is causing competitive harm in the market.

D48. Following Eircom's point that the modification / withdrawal of a non-compliant bundle within ten weeks may not be possible where a reduction to standalone price of retail line rental and the associated SB-WLR price must be notified to ComReg two month's in advance, ComReg agrees with Eircom that Eircom would be left with no more than 2 weeks to propose a modification to a non-compliant bundle and to obtain ComReg approval. ComReg believes this is feasible. However, ComReg cognisant of Eircom's point and that the required seven week notification to OAOs for any such amended SB-WLR price cannot be waived, ComReg will extend the period by which modification / withdrawal must be complete from 10 weeks as proposed in Consultation Document No. 10 / 01 to 12 weeks which will be reflected in the draft Direction in this consultation. ComReg recognises that Vodafone called for a shorter modification / withdrawal period. However, ComReg considers that a shorter period cannot be mandated given the existing notification requirements for the retail and wholesale component products within bundles e.g. if Eircom reduces the price of SB-WLR to make a bundle reasonable, this would require 2 months notification to ComReg pursuant to D07 / 61.

D49. Following Eircom's point that ComReg's proposal to pre-clear correspondence by Eircom with its affected customers on the non-compliant bundle would remove from Eircom a basic commercial freedom and has no justification, on further consideration ComReg agrees to remove this from the direction.

Other issues?

D50. In Consultation Document No. 10 / 01, ComReg sought views from respondents on any issues not considered by ComReg:

Consultation No.10 / 01 Question

Q.5. Are there any issues in relation to the further specification of obligation not to unreasonably bundle that ComReg has not considered in this consultation? If so, please document and explain those issues fully and provide examples where appropriate.

Views of Respondents

D51. **BT** notes their concern that there would appear to be little downside to Eircom in launching an inappropriate bundle whilst for their competitors there is significant downside as set out by ComReg in Consultation Document No.10 / 01. BT notes that it would seem that the balance of power lies with Eircom which BT believes is not conducive to the development of full and sustainable competition in Ireland. In this regard, BT notes ComReg's latest quarterly market report that indicates that Eircom's market share in the relevant narrowband market has remained stubbornly high. BT also notes that ComReg is currently constrained in its ability to levy fines on Eircom for unreasonable bundling.

D52. **Vodafone** notes that Eircom has advised the industry that it intends launching an SDSL product based on its NGN capability before the end of 2010. Vodafone considers that where this is used to provide connectivity to Eircom's voice platforms it falls within the Retail Fixed Narrowband Access Market. Vodafone believes that ComReg should set out the manner in which bundles which incorporate such access will be treated so that there is market certainty and to avoid situations where ComReg is faced with reactive interventions which would allow Eircom first mover advantage as an SMP operator.

D53. Vodafone also has concerns in relation to the transparency around ComReg's review of bundles submitted by Eircom for approval. At present, Vodafone states that there is no means by which competing operators can know if a particular Eircom bundle coming to the market is compliant or not. Vodafone considers that OAOs cannot get clarity as to its regulatory position of a bundle since ComReg does not report on the actual process for a bundle and has not to date clarified the matter in respect of specific bundles even if requested to do so. Vodafone notes that this means that Eircom are the only player in the market with regulatory certainty as to the compliance of any particular bundle. Vodafone believes that this clearly conveys a competitive advantage on Eircom and discriminates against OAOs. For example, Vodafone notes that OAOs could launch a competitive response to an Eircom bundle on the assumption that it is compliant as Vodafone states that there is no point seeking clarification from ComReg since this will not be forthcoming. However, Vodafone notes that if Eircom have failed to submit it for approval and are subsequently instructed to withdraw the offering, OAOs will already had invested significantly in a competitive response to a non-compliant bundle. On this basis, Vodafone notes that this investment will then have been unwarranted and may well be totally wasted.

D54. **Eircom** notes that it fails to understand why ComReg persists in addressing the margin squeeze test for bundles in separate "silos" for a narrowband and broadband, which does not contribute to either efficient administration or regulatory clarity. Furthermore, Eircom states that if ComReg proposes to apply the no unreasonable unbundling rule to Eircom on the basis of bundles containing both retail-minus and cost-plus regulated components, then Eircom believes that ComReg must apply the same principles and rules to any bundled offering that involves SMP components. Eircom considers that this would include any bundle involving wholesale mobile termination or fixed termination where the party offering it has been designated as an SMP provider. Eircom believes that any other treatment would be unfairly discriminatory against Eircom and Meteor.

D55. Finally, Eircom believes a number of important legal and policy issues are raised by ComReg's proposed test and procedures.

Direction

D56. In Consultation Document No. 10 / 01, ComReg sought views from respondents on the draft text of the proposed direction:

Consultation No. 10 / 01 Question

Q.6. Do you believe that the draft text of the proposed direction is from a legal, technical and practical perspective, sufficiently detailed, clear and precise with regards to the specifics proposed? Please explain your response and provide details of any specific amendments you believe are required.

Views of Respondents

D57. **BT** believes that the draft text of the proposed direction is sufficiently detailed, clear and precise.

D58. **Vodafone** suggests the following is added to section 3.8 of the direction:

i. Immediately cease the addition of any new customers to the designated ‘unreasonable’ bundle.

D59. **Eircom** states that the draft direction incorporates a proposed test that Eircom believes is plainly incompatible with ComReg's statutory objectives and fundamental notions of fairness and natural justice. Eircom believes that the application of an ATC test at a highly granular level is completely disproportional, will unfairly discriminate against Eircom and will distort competition in the marketplace. Eircom believes that the direction will require substantial revision in regard to the cost standard applied, how it applies, and the review process.

D60. Eircom notes that some points that are clearly missing from the direction and will need to be addressed. Those points are as follows:

- Section 3.8 should include an additional category: “any other corrective action that is mutually agreed by ComReg and Eircom”.
- The timing, focus and scope of the competitive assessment that is mentioned in section 3.3 should be clarified, in particular to stipulate that the particular competitive dynamics associated with each particular bundle will be assessed (and not simply the overall state of competition in the Irish telecommunications marketplace).
- Definitions of key terms used to specify the meaning of the terms used in applying the net revenue test should be included, subject to the application of a “fair and reasonable” standard in the given context in all cases in which the terms cannot be defined precisely in advance. Eircom considers that ComReg should make clear that the default will not automatically be the definition that yields the highest cost floor possible for Eircom, but rather the definition that will best promote consumer welfare, innovation and investment by Eircom and others.
- A procedure and criteria should be included for evaluating the appropriate cost stack or combination of cost stacks (ULL, WLR / LS, or WLR / WBA (Bitstream)) that should be used in determining the appropriate wholesale input value for broadband, reflecting actual market conditions.

- If ComReg does not adopt AAC as the relevant cost standard for assessing the profitability of bundles, the direction should include a clear set of procedures and criteria for re-examining the issue.
- Timing, criteria and procedures for re-assessing the need and justification for an ex-ante margin squeeze test for bundles should be set forth in the direction.

Regulatory Impact Assessment

D61. In Consultation Document No. 10 / 01, ComReg sought views from respondents on the draft Regulatory Impact Assessment:

Consultation No. 10 / 01 Question

Q.7. Do you have any views on this Regulatory Impact Assessment and is there other factors (if any) ComReg should consider in completing its Regulatory Impact Assessment? Please explain your response and provide details of any factors that should be considered by ComReg.

Views of Respondents

D62. **BT** agrees with the Regulatory Impact Assessment and has no further views.

D63. **Vodafone** believes that as part of the RIA, ComReg should consider the impact of the proposal to allow 10 weeks for Eircom to withdraw or amend an unreasonable bundle. Vodafone believes that the 10 week period is excessive and one which have negative impacts on competition and consumer welfare.

D64. Eircom considers the draft RIA does not accurately reflect the material adverse impact or the discriminatory effect that the preliminary proposal set forth in Consultation Document No. 10 / 01 would have on Eircom. Eircom believes that if the proposed test and review process are modified as proposed by Eircom, and applied to all bundles involving SMP components (regardless of operator), Eircom has no doubt that a defensible RIA will result.

ANNEX E: Consultation Questions