Commission for
Communications Regulation

Submissions received in relation to Consultation

Setting a Maximum Local Loop Unbundling ('LLU') and Sub Loop Unbundling ('SLU') Monthly Rental Charge

Submissions received from respondents

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Response to ComReg Doc. 09/39:

"Response to Consultation Document No 08/56 Further Consultation on Local Loop Unbundling ('LLU') And Sub Loop Unbundling ('SLU') Monthly Rental Charges"

eircom

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APPENDICES.

OVERVIEW

This document constitutes eircom's response to ComReg's Consultation Document 09/39 (*"Response to Consultation Document No 08/56 Further Consultation on Local Loop Unbundling ('LLU') and Sub Loop Unbundling ('SLU') Monthly Rental Charges")*.

This Consultation is the most recent step in a process which ComReg initiated in 2007 to review eircom's LLU and SLU monthly rental prices by building a bottom-up model of eircom's access network.

ComReg is proposing a fundamental change of approach to LLU price setting in Ireland as it proposes to abandon the use of the geographically averaged costs of eircom's local access network as the basis for LLU pricing in favour of a methodology which weighs the costs of the local exchanges depending on their probability to be unbundled. A cut-off point is set at exchanges serving 1,600 working lines or more. A 95% weighting to the cost of the 68% of lines that fall into this category is applied, and a 5% weighting to cost of the remaining 32% of lines. A price of €12.18 per month (compared to €16.43 today) is calculated on the basis of this "national" weighted average cost of lines likely to be unbundled, using a bottom-up LRIC model that computes a nationally average monthly loop cost of €16.52 across a 36 month price control period starting on 1st July 2009.

eircom has a number of significant reservations with regard to ComReg's analysis and the proposed methodology:

- ComReg's analysis overlooks the centrality of LLU as a physical and pricing input into eircom's regulated access network products such as Wholesale Line Rental and Retail Line Rental. In addressing the price of ULMP in isolation of these and other issues such as the ongoing price of Line Share and the knock-on effects on eircom's overall cost recovery, it has focused too narrowly on the impact of reducing one price, in one market, without a holistic consideration of the wider impacts of other relevant prices in other relevant markets.
- eircom's pricing policy is national in scope, for the benefit of all consumers in Ireland including those situated in rural areas. eircom's retail prices recognise the costs of eircom's entire local access network..ComReg's proposal, based as it is on a weighted average cost, strongly skewed towards those exchanges that ComReg believes are likely to be unbundled, strikes at the heart of this approach. There is insufficient consideration given to the impact of this and in particular on the consequent impact on customers outside the areas covered by exchanges likely to be unbundled.
- ComReg states that "OAOs *should* [not] *be required to pay for the cost of lines that they would not be prepared to unbundle*" (para 3.156, p. 25 of 09/39) and that it is "*important and proportionate to take account of the fact that some lines or exchanges are less likely to be unbundled by OAOs*" (para 5.3, p. 67 of 09/39). It is not entirely clear how this policy, obviously designed to lower current LLU price, will assist in promoting competition including ensuring maximum consumer benefit in terms of choice, price and quality and encouraging efficient investment in infrastructure. In view of the centrality of LLU as a cost input into other retail and wholesale products, ComReg's singular objective to reduce the LLU price regardless of consequences risks the potential for a significant damaging impact on eircom and other stakeholders and the competitive structure of electronic communications markets.
- ComReg's scant and dismissive consideration of a USO Fund in the context of its proposal appears to ignore the fundamental and intrinsic relationship between its assessment of those exchanges "likely to be unbundled" and the net cost of the universal service provision, making it impossible for eircom and other stakeholders to fully understand the implications of the proposal. Why should the cost of a universal service be borne solely by eircom's customers but not those of OAOs? This does not appear to be consistent with the very idea of a universal service and its funding. It is not acceptable that ComReg can seek to sidestep an issue of such significance by saying that it will consider any request for funding that may arise. ComReg's proposals will entail a funding deficit for the universal service provision for which eircom will have to be compensated. In the absence of a clear approach to such issues, neither eircom, as the universal service provider, nor other operators (who may be required to contribute to the fund) can properly assess the merits of ComReg's proposed pricing approach.

- ComReg's Regulatory Impact Assessment fails to consider very significant issues and as such does not meet the minimum requisite standard for an RIA appropriate to a decision of such significance on stakeholders and on relevant markets. This not only amounts to an error of process, but an inadequate RIA carries the substantial risk that not all policy options will be explored and/or that the wrong policy will be selected. In this response, eircom will set out how ComReg should approach an RIA in the context of this Consultation.
- eircom also believes that ComReg cannot adopt such a fundamental change in both the methodology to determine LLU pricing and the price directed without first conducting and completing its review of the relevant market for the provision of local loop unbundling (now known as WPNIA). eircom notes that as recently as 6 March 2009 in a letter to Ofcom, the European Commission made it clear that it was not appropriate to notify a remedy or amend regulatory obligations several years after the relevant market analysis without carrying out a new market review. In the Commission's view, this carries a risk that the measures will be based on a market definition or an SMP assessment that does not correspond to the current market situation, or that the remedies will no longer be appropriate to the problem identified, proportionate or justified. This risk is clearly significant in relation to the provision of LLU in Ireland in view of the scale of the change in approach proposed by ComReg.

eircom in addition continues to have significant concerns with the model which ComReg proposes to use to arrive at a cost-oriented price. eircom has engaged at length with ComReg in relation to it. Throughout this process, ComReg has already addressed many of the eircom concerns with the model and its inputs. However serious issues remain unresolved:

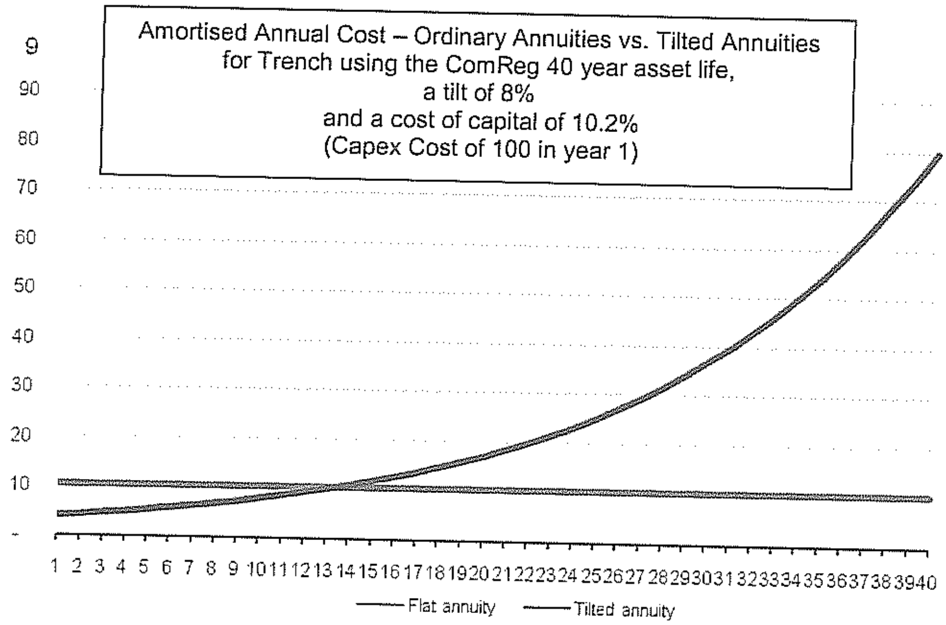
- ComReg has set out to develop a complex bottom-up engineering model of a new national copper network. The output of this modelling is an estimate of the total CAPEX and OPEX required to efficiently replace eircom's copper network. Outputs of the model are used to inform the Consultation at a time where the model has not been finalised and materially significant methodological issues remain outstanding. This means that the prices set out in Doc. 09/39 are susceptible to significant variations and accordingly are potentially misleading. This is all the more the case since prices produced by ComReg's methodology are highly sensitive to both the total CAPEX cost modelled, and to the rules used to amortise these costs. eircom notes that regrettably ComReg has not engaged, let alone consulted, on significant underlying accounting and economic principles.
- Distorting and arbitrary methodologies are used to convert capital costs into prices. These concerns can be categorised as follows:
  - **temporal effects** (tilted annuities and future volume) - these very substantially reduce the average amount to be charged per month for a loop in the initial 3 year period of the price control
  - **geographic effects** (threshold for unbundling and probability weighting) – these involve arbitrary choices of limits on categories of exchange, length of lines and the probability of any category being unbundled, and thus provide ComReg with significant latitude to vary the price for ULMP over an extremely broad range.

Temporal Effects

The use of a tilted annuity methodology for amortising capital cost means that the recovery of the network is either accelerated or deferred compared to an ordinary annuity such that the profile of cost recovery simulates that which would be achieved in an open and competitive market. Tilted annuity methodologies are frequently used in context of the recovery of core network costs, in which technologies tend to have relatively short economic lives and to be subject to progressive functional obsolescence. Where functional obsolescence contributes, inter alia, to deflationary price trends over time, the input of such trends to the tilted annuity formulae results in a recovery profile that is tilted downward, with higher charges in early years. This approach provides for a forward loaded recovery of costs coincident with the period of greatest economic value.

The use of a tilted annuity methodology for amortising capital cost means that the recovery of the network is either accelerated or deferred compared to an ordinary annuity. The access network is characterised by assets with very long economic lives (ComReg has recently proposed to direct a regulatory asset life for trench, the dominant asset category by value, of 40 years, and has based its current Consultation on these extended asset lives). ComReg is arguing that, because trench and other access network assets are primarily capitalised labour cost, the value of these assets will continue to increase year on year by ComReg's view of the long term trend in construction costs. The effect of this is to defer the recovery of the capital costs as illustrated in the chart below. In the three years of the price control eircom will only recover 40% of the modelled capital costs which would have been recovered if the charge were calculated using ordinary, or flat annuities.

eircom believes that given the sensitivity of the price to the method of annualisation chosen and to the inputs used in the annualisation computation that ComReg should consult further on this issue. For each asset class ComReg should put forward its reasoning as to which method of annualising costs most closely approximates economic depreciation and what are the appropriate input values for computing the annualised cost for that method. ComReg should be open to the possibility that different asset classes will require different annualisation methodologies and differing input values.



eircom notes that implicit in ComReg's use of tilted annuities is that there will be significant increase in the ULMP price, in future years. The implications of this have not been articulated despite the fact that stakeholders have a direct interest in understanding these implications.

The directed price is an average of values from the model for a three year period from mid-2009 to mid- 2012. The model suggests a substantial price rise will need to apply in 2012[redacted].

[redacted]

Geographic Issues

A significant factor in ComReg's approach to setting the *price* for the provision of LLU by eircom is the selection of thresholds (for exchange size and line length) beyond which unbundling is unlikely to occur. It appears to eircom that ComReg's selection is rather arbitrary and/or that no adequate reason, as against the objective being pursued by ComReg, has been provided for ComReg's choice of 1,600 lines for exchanges or a line length of 5 km. This is also the case of the 95/5 probability factors. Although ComReg claims to have a theoretical justification for these ratios, they appear arbitrary and amenable to change at any point in time.

The absence of an adequate justification by ComReg for these choices against the objectives being pursued makes any future assessment of such a fundamental change of approach impossible and accordingly, the regulation of LLU pricing in Ireland unpredictable and thereby potentially detrimental to consumer welfare. It also makes it impossible to understand the reasons for such a fundamentally new approach to LLU pricing and to reconcile it with the approach followed to date in relation to LLU or other wholesale products. Previous LLU prices computed on the basis of nationally averaged costs were considered to be adequate for the purpose of cost-orientation (D15/04 refers) while in relation to interconnect prices, costs are required to be averaged based on taking account of eircom own use volumes. It is not entirely clear why this should no longer be the case for LLU.

Finally, ComReg's analysis fails to take account of the ongoing reduction in the number of access lines, which is particularly acute in the current economic recession, and the impact of this on overall costs. In particular, it has failed to address, in sufficient detail, the impact of reducing access line numbers, when taken together with the Draft Direction with regard to the Line Share price, on eircom's ability to recover its costs. eircom's forecasts are broadly in line with experience in other EU and OECD countries, where fixed line volumes are declining. ComReg's forecast of constant volume has no basis in fact, and appears to have as a sole reason ComReg's objective to generate a lower price than would otherwise apply.

Furthermore, ComReg's treatment of future volumes does not address the realities of ongoing losses in lines and the consequent increased cost per line, giving dis-economies of scale as lines are lost. ComReg also has made no allowance for the likely geographic concentration of line loses in urban areas where platform competition is most intense. Within the period of the price control, these effects may be relatively modest compared to the other factors, but looking to the longer term, a proper appreciation of the impacts of falling volumes – and the impact that the higher charges indicated by the model may have on such volumes - will be essential for understanding issues such as Line Share and USO.

RESPONSE TO CONSULTATION QUESTIONS

Forward-Looking Trends – Copper and Other Asset Prices

Q. 1. Do you agree that the period from 2000 to 2012 is a reasonable length of time to evaluate the price trend data for the copper access network assets? Please state the reasons for your response.

Q. 2. Do you agree that the basis used for forecasting price trends for copper and the other local loop assets (i.e. poles, trenches, chambers, MDFs, street cabinets, etc) appears reasonable? Please state the reasons for your response.

eircom is sceptical of the appropriateness of using tilted annuities as a methodology for annualising capital costs for the reasons set out elsewhere in this document. Where a convincing case can be made for a particular Asset Class that tilted annuity provides a reasonable proxy for economic depreciation, then the tilt chosen should reflect the changing value of the output from that asset over its economic life.

ComReg has provided no evidence, for any Asset Class, that tilted annuity provides a good proxy for economic depreciation. Where a convincing argument could be made for using tilted annuity, the appropriate tilt is specific to each individual Asset Class and is a function of the asset's economic life and the rate of technological progress associated with that asset. There is no reason to believe that any particular time period over which price changes are measured would provide a universal guide to the appropriate tilts of all the different Asset Classes in the access network. Furthermore, it is impossible to know if the period 2000 to 2012 is an appropriate period over which to measure price changes, as the price changes between now and the end of 2012 are unknowable until the end of the control period.

Forward-Looking Trends - Contractor costs

Q. 3. Do you agree that it is reasonable to consider that contractor costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

Forward-Looking Trends – Labour Costs

Q. 6. Do you agree that it is reasonable to consider that labour costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

To the degree that these inputs influence the tilts of assets used in the tilted annuity formula please see the answer to questions 1 and 2.

To the degree that these inputs influence the capital value of assets modelled as built in future periods eircom does not accept the values ComReg has used in its modelling.

eircom has previously submitted its views on these issues to ComReg through previous submissions and bilateral engagements and has not changed its position.

Forward-Looking Trends - Working lines volumes

Q. 4. Do you believe that the volumes of working lines will increase, decrease or remain static over the proposed price control period? Please state in percentage (%) terms your views on the likely movements with detailed calculations, if necessary.

[redacted] eircom vigorously disagrees with ComReg's assertion that net line loss will cease within the next twelve months. This arbitrary deviation from the forecast provided by eircom, for which ComReg has provided no empirical justification, appears inconsistent with all reputable economic forecasts of the severity and duration of the current economic crisis in Ireland.

eircom has provided a forecast of volumes based on the extrapolation of observed trends from the recent past. It is very likely that these historic trends do not adequately capture either the scale of the economic contraction (e.g. in early June 2009 Goodbody's Stockbrokers issued a report[1] forecasting that unemployment will peak in 2011 at 17.5%, long after ComReg has decided our line loss will have stopped), or the emergence of competing platforms. Platform competition is particularly important. At the time that eircom provided ComReg with its forecast, UPC (Chorus/NTL) had only just launched its aggressive push into telecommunications services in Dublin and other urban areas through its "Line rental is dead" campaign. In other countries where UPC operates, it typically achieves a telecommunications penetration of the order of 35% of homes passed by its network. [redacted]

Furthermore, UPC is only building a digital cable network in urban areas and its network footprint is almost exclusively contained within the exchange areas above ComReg's 1,600 working lines threshold for probable unbundling. Given the much greater weighting given to lines in these areas by ComReg, there is a structural deficiency in the modelling in that it cannot account for geographically concentrated line loss. Indeed, ComReg's methodology for distributing forecast working lines to MDFs in proportion to known volumes of lines passed per MDF explicitly and erroneously assumes that all MDFs will be subject to similar proportions of line loss.

There is an inconsistency in the approach ComReg has taken to future volumes and the recovery of capital costs through the use of tilted annuities. Given the parameters that ComReg has set for computing the tilted annuities, the monthly ULMP charge will have to rise over time if the modelled capital is to be recovered on this basis. Only in the utterly implausible scenario that the demand for copper loops is completely insensitive to price will there not be a reduction in volumes associated with increasing prices at faster than the rate of inflation. Rising annualised asset cost recovery in combination with declining volumes would result in exponentially rising costs per line per month. Nowhere in the consultation process does ComReg appear to have considered how plausible it is to assume that costs can be recovered on this basis over the medium to long term.

[1] http://www.rte.ie/business/2009/0610/economy.html

Working Capital

Q. 5. Do you agree with ComReg's preliminary view that working capital should not be included in the BU-LRAIC cost model used to determine the LLU monthly rental charge? Please state the reasons for your response.

eircom does not agree that working capital should be excluded from BU cost models. This issue has been dealt with extensive in bilateral correspondence[redacted] and eircom has not changed its position.

Forward-Looking Trends – Labour Costs

Q. 6. Do you agree that it is reasonable to consider that labour costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

Question 6 is answered in conjunction with question 3 above.

L.F.I.

Q. 7. Do you agree that the LFI of the current Eircom network is not an appropriate basis on which to set the operating costs of a BU-LRAIC model in determining the LLU and SLU monthly rental charge? Please state the reasons for your response.

Q. 8. Do you agree that the LFI of an efficient BU-LRAIC model, used to determine the LLU and SLU monthly rental charge, should be based on an LFI not exceeding 8%? Please state the reasons for your response.

eircom has proposed to ComReg to build a bottom-up model of the operating costs for the copper access network modelled by TERA for ComReg. As the network modelled includes cable capacity in line with eircom planning rules, and includes the costs of final drops for projected new demands over the price control period, eircom finds that the main direct cost of operating that network is the cost of clearing faults.

eircom has used a bespoke workforce planning tool to model the staff resource required to clear the projected level of faults in line with the USO service assurance targets determined by ComReg in D02/08 published in May 2008. In that Decision ComReg determined that eircom must improve the Line Fault Index (LFI) from the level reported at 2007 to 12.5% by the end of June 2012.

eircom believes that the model for the operating costs used in conjunction with the LRIC model of the capital investment in the copper access network should be consistent with LRIC principles. The primary LRIC principle is that the view of costs to be taken is "long run" – that is that investments are viewed over the life of assets deployed and that costs are recovered over those lives using economic depreciation or some other form of annualisation.

In the discussion leading to questions 7 and 8, ComReg proposes that an average LFI lower than 12.5% is temporarily achievable in areas where network has recently been built or renewed. However, in exactly the same way as the (high) capital costs are not recovered from LLU prices only in the early years of the investment, so the (low) level of operating cost modelled for the early years of a newly

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[redacted]

built network are not an appropriate basis for LLU price setting. Consequently eircom finds that the model for operating costs that should be used in conjunction with the LRIC model for the investment should reflect the costs of operating a network where the assets are aged by 50% of their regulated asset lives on average.

The line fault index of 12.5% used by eircom in modelling the manpower resource required to deliver USO targets for fault clearance is a national average and is based on historic fault arrival patterns. The fault arrival rate in any given area is, in part, due to the age of the network but is primarily driven by the exposure of that network to the elements, or to other interference. In rural areas the predominantly overhead distribution is more exposed – and comprised of assets that must be replaced more regularly. In urban areas the underground distribution provides better protection for assets that then require less regular replacement. So the fault arrival rate will always be lower in urban areas.

However eircom cannot agree that a nationally averaged rate for LFI of no more than 8% is the appropriate basis for modelling the long run cost of operating the modelled access network. eircom notes that this performance level is much more demanding than the level of service set by ComReg for the long term USO fault occurrence target.

A level of 8% is lower than that experienced by most national operators, many of whom are dealing with a network that contains more underground network than is deployed in actuality by eircom or than that produced by the ComReg bottom-up model.

As the direct manpower costs, and so the overall level of operating costs, modelled by eircom reflects the regional variation in LFI, the modelling approach captures the lower costs per line of operating the urban, and newer, portions of the network. This has been implemented in the OPEX module by calculating the direct operating costs separately for 40 service assurance team areas. Each team area has a separate LFI based on historic fault arrival rates adjusted for network improvements. The staffing of each team is set to deliver the USO fault clearance performance at the target arrival rate and the operating cost for the MDFs within the team area is modelled based on this staffing. So the operating cost for a large urban exchange is based on a fault index well below the national average of 12.5%. The weighting approach proposed by ComReg for ULMP monthly rental price setting at paragraph 5.28 of applying a 95% weighting to exchanges larger than 1,600 lines and a weighting of 5% to exchanges below 1,600 lines reduces the fault index used to set the LLU rental actually below 8%.

<u>General Questions – Overall Approach</u>

Q. 9. Do you agree with the overall preliminary approach taken by ComReg above in relation to the basis used in determining the capital costs and operating costs used in the BU-LRAIC model for determining the monthly rental charges of LLU and SLU services in Ireland? Please state the reasons for your response.

For reasons that are made clear in the other sections of this response, eircom does not agree with ComReg's proposed approach, as outlined in Consultation 09/39.

Fault Clearance Charge

Q.10. Do you agree that the fault clearance charge should remain a separate charge from the LLU monthly rental charge? Please state the reasons for your response.

We note the proposed rental prices, and modelling approach, exclude fault reporting and clearance costs. eircom agrees that the fault clearance charge for unbundled loops should remain separate from the LLU monthly rental. eircom considers that the separate fault reporting charge should also be retained. eircom takes this position for three reasons:

- A charge for fault clearance of unbundled loops separate from the monthly rental charge encourages efficient behaviour by OAOs in reporting faults to eircom
- As eircom reduces the LFI, the price structure proposed for LLU services will allow OAOs to benefit from improved eircom efficiency
- The existing price structure has operated successfully for a number of years and eircom has detected no demand for a change that would, in any case, lead to an increase in monthly rental

When an OAO unbundles an eircom loop, the copper path is connected to the OAO equipment and this equipment will generally support the testing of the copper path as well as the equipment supported in the customer premises. eircom no longer has any remote capability to test the unbundled path for fault conditions. When the OAO service is reported faulty, the OAO equipment located in the eircom exchange will indicate the likely location of the fault – either at the equipment in the eircom exchange, in the eircom copper path, or in the customer premises. If the fault is located in the first, or the last, of these the OAO must make their own arrangements for fault clearance and any reporting of such faults to eircom will result in an unproductive despatch of a field team member to test the copper path. The implementation a separate charge for fault clearance provides the OAO with a strong economic incentive to make efficient use of the test data – and prove the fault out of their own equipment before reporting the fault to eircom. In addition to this, eircom provides an additional price signal for efficiency by charging at a lower rate for fault clearance where the OAO provides eircom with the electrical measurements from the test that proved the fault into the copper path.

The level of the modelled operating costs to be recovered from the proposed LLU rental charge has been reduced by an amount equivalent to the product of the fault clearance charge and the recent observed LFI for the region where the path is located. Initially the OAO will expect to be charged separately for faults at this rate. As the eircom programme of interventions to meet the USO glide path for LFI takes effect, the OAO will see the occurrence of fault clearance charges decline and the total cost of operating the unbundled path will fall. If the LLU rental is simply set to recover the modelled level of operating cost, the cost to the OAO of operating the unbundled path will stay at the same level through the control period even when eircom actions reduce the LFI – without a further review of the LLU rental charge.

Established LLU processes for fault reporting and clearance are built around the price structure with the separate charges. These are well understood by industry and operate efficiently. OAOs appreciate that the charge encourages efficient operation, and eircom believes that they prefer this structure to one with a higher line rental.

De-Averaging

Q. 11. Do you agree that exchanges with working lines in excess of 1,600 is a reasonable cut-off for those exchanges that are unlikely to be economically viable for OAOs to unbundle in the timeframe of the proposed price control period? Please state the reasons for your response.

eircom does not agree that

- Any exchanges should be excluded from the cost calculation
- That number of lines alone is the correct indicator of probability of unbundling
- That 1,600 line cut-off has any robust basis, given the proposed price.

The proposed methodology is flawed in logic and application, uses arbitrary and poorly referenced assumptions, and the implications of its implementation for the development of a competitive retail Broadband market in rural Ireland are extremely serious. This issue is set out at some length in Appendix 1.

eircom cannot accept the principle of excluding any proportion of any subset of lines from the calculation of a nationally average price, *unless an explicit, credible and robust mechanism* is put in place to enable eircom to recover the cost of those lines excluded from the calculation for LLU pricing purposes. Absent such a mechanism, eircom rejects the principle and its application in the context of LLU pricing. ComReg proposes that a USO fund might be addressed at some point in the future, but absent such a mechanism, ComReg's proposals are simply not sustainable in the medium term.

To the extent that ComReg seeks to 'deaverage' prices by reducing prices in exchange areas likely to be unbundled to reflect costs in such areas but seeks to maintain the average price in higher cost areas then it is axiomatic that a funding deficit will exist and that eircom, as the USO operator, is entitled to the benefit of a USO fund to ensure that it can earn its requlated rate of return. It is not acceptable that ComReg can seek to sidestep an issue of such significance by saying that it will consider any request for funding that may arise. It must openly acknowledge that a deficit will arise and set out how it will respond to the funding request which will inevitably follow including how it would propose to finance and guarantee the USO fund and address timing and payment issues. In the absence of a clear approach to such issues neither eircom, as the recipient of fund proceeds, or other operators (who may be required to contribute to the fund) can properly assess the merits of ComReg's proposed pricing approach.

Exclusion of Long Lines – 5 km Limit

Q. 12. Do you agree that it is unlikely that an OAO would unbundled a line unless it was able to provide Broadband services over that line; and do you agree that 5km represents the maximum line-length that may be used for those services? Please state the reasons for your response.

Q. 13. Do you agree that ComReg's proposal is conservative in that it includes an element of the costs associated with lines in excess of 5km?

eircom does not agree that an OAO is unlikely to unbundle a line unless it is able to provide a Broadband service over that line.

It is probable that an OAO would not unbundle any exchange, unless it intended to offer broadband service. Having unbundled a site, the OAO is likely to offer voice services. If a specific line in an unbundled area could not support a broadband service, it may still be economic to offer voice only service.

At the range of price points proposed by ComReg for ULMP the OAO locating equipment at an eircom MDF will receive a contribution of almost €6 (€18.02 - €12.18) per month to the costs of provision of their own PSTN service – when compared with the SB-WLR charge that they now face to provide service to customers using the eircom wholesale variant. An OAO deploying a subscriber access module (xSAM) with "combi-cards" can choose to provide PSTN, PSTN and Broadband, or stand-alone Broadband on any line. Once the OAO has made the fixed investment in locating this equipment at the eircom MDF – and the investment in providing their own PSTN service to sell alongside Broadband - they will sell this service to any retail customer that does not have a requirement for fixed Broadband.

eircom does not agree that 5 km represents the maximum line length that should be used for the provision of PSTN or Broadband services. In general, the provision of PSTN and Broadband services over a twisted copper pair are limited by a combination of noise and attenuation. Both of these are influenced – but not uniquely determined – by the line length. For instance, provincial and rural overhead copper networks use a heavier gauge of copper per pair than is used in urban networks giving a lower attenuation per kilometre. In a similar way noise from crosstalk between multiple pairs in the same cable binder may be the factor that limits the reach of urban Broadband services. In provincial networks with overhead distribution the smaller number of pairs per binder results in lower levels of crosstalk and a greater reach for services. External sources of noise may also affect the reach of Broadband services but these may originate at any point on the intervening network and are only statistically more likely to affect longer lines – and do not lead to a cut-off by cable length. In the provision of eircom's own Broadband and Bitstream services this mix of factors has been recognised by making the services "rate adaptive" such that they can adjust the throughput to deliver the best achievable service given local conditions. This implementation has resulted in stable Broadband service provided over many pairs longer than 5 km. On the eircom network, 62dB is the average attenuation observed for lines of 5 km. Some 10.34% - or 155,000 of the 1,509,000 lines connected to DSL enabled eircom MDFs - have attenuation greater than 62dB and are thus assumed to be longer than 5 km. Of these 55,000 support a Broadband service. Even if only Broadband capable lines are to be unbundled – a proposition that eircom does not accept – the weighting that ComReg has proposed does not reflect the probability that a line longer than 5km will actually be unbundled.

[redacted] ComReg claim that large exchanges should have 1.3% of lines longer than 5km, and that these long lines are 6.4 times less likely to be unbundled than shorter lines. ComReg therefore gives such lines a weighting of 0.2%. eircom accepts that longer lines may be less suitable for higher speed broadband, but considers ComReg has not used the correct parameters. The actual experience in the eircom network today, in exchanges which are already unbundled, and in those sites with more than 1,600 lines, is that over 6% of lines are longer than 5km, but these make up over 4% of all broadband or unbundled pairs. The weighting, based on reality of the current position in larger sites, is 4%, not 0.2%. For the avoidance of doubt, eircom does not support the exclusion of small sites.

[redacted]

In summary, eircom disagrees with the ComReg proposal to recover only the costs of loops up to 5 km from the ULMP price for two reasons. There is a strong economic rationale for an OAO unbundling eircom loops to provide a PSTN service over at least some of those loops, and PSTN can be provided over loops well in excess of 5 km. Where the OAO provides a full range of Broadband services over eircom loops the history of Bitstream provision shows that such services have been provided to customers served over loops longer than 5 km. eircom finds that the OAO currently serving this customer using Bitstream will expect to be able to migrate this customer to LLU provision after making the investment at the serving MDF.

As regards question 13, if the lines longer than 5km were to be excluded, eircom finds that the ComReg proposed treatment of the cost elements to be excluded is broadly consistent with LRIC principles. This is the case because ComReg and TERA have analysed the network costs that would be incurred if the network only extended to buildings that could be reached with copper paths of up to 5km length. ComReg and TERA have also modelled the network costs that would be incurred if the network only extended to all buildings. The cost that is excluded is the difference between the two costs modelled. This approach is consistent with LRIC as the service increment removed is the provision of service to buildings beyond 5 km – and the cost removed is the incremental cost of additionally serving those buildings.

However, as laid out above, there is no basis for systematically excluding the costs of lines longer than 5 kilometres from those to be recovered from LLU rental revenues. ComReg has not taken any account of the actual situation with broadband lines in Ireland today. It is not possible to say the treatment is "conservative" without considering the facts. But whether the proposal for excluding the costs associated with that group of lines is conservative or otherwise is moot, as the exclusion is fundamentally unjustified.

Large vs. Small Exchanges and Exclusion of Long Lines - ComReg Proposed Weightings

Q. 14. Do you agree with ComReg's proposed weightings, as set out above, used in relation to the cost associated with long lines and small exchanges? Please state the reasons for your response.

eircom does not agree with ComReg's proposed weightings in relation to the treatment of the costs of long lines and small exchanges for the purposes of setting the price for LLU monthly rental. eircom finds that the selection of the two figures central to the weighting calculation is entirely arbitrary. The first arbitrary selection is the cut-off at 1,600 lines as the definition of the boundary between "large" and "small" exchanges. The second arbitrary selection is the figure of 95% weighting for the average cost of unbundling "large" exchanges - and the associated 5% weighting for the cost of small exchanges.

We have referred to the issue of the 1,600 line "cut-off" above. ComReg refers to the weighting (e.g. in section 5.4) as a "probability weighting". ComReg should be very clear what probability is being considered. ComReg is not alleging that every exchange with more than 1,600 lines has a 95% probability of being unbundled. If this was the meaning, there would be no need for the probabilities to add up to 100%. It would be quite feasible for one to consider three groups of exchanges with different probability. Those already unbundled would have 100% probability of being unbundled. Other large sites could have 70% probability of being unbundled, and small sites would have 10% probability. With this approach, there is no need for the probability to add to 100%.

It appears that ComReg is proposing that a randomly selected unbundled line has a 95% probability of being in a large exchange, and a 5% probability of being in a small exchange. Given that only 32% of all lines are in smaller sites, there is a higher probability (over 10%) of such sites being unbundled.

The application of 95% probability for unbundled lines as being served from a "large" exchange also seems to have no basis other than having been used by ARCEP in France. No evidence is presented as to why this probability is appropriate. It does at least have the merit that it cannot be adjusted too far in the upward direction: it could not be greater than 100%, but an arbitrary figure of 99% would be even more defensible in this regard.

The adjustment factor of 6.4 for long lines is based on the fact that ComReg is allowing for 5% of lines unbundled to be in small exchanges, which contain 32% of the lines. Having made an arbitrary decision about small sites, ComReg is careful to make a consistent, but exactly equally arbitrary decision about long lines. ComReg therefore assumes only 0.2% of unbundled lines in large exchanges are more than 5km. ComReg has not compared this assumption with the reality that 4.1% of current Broadband lines in service lines in existing unbundled exchanges are longer than 5km. Indeed the OAOs locating equipment in those exchanges have rented eircom loops such that 4.2% of their ULMP lines are longer than 5 km. As can be seen from the data tabulated in Table Q12 above 6.4% of lines connected to the current LLU exchanges are longer than 5km. So the correct probability weighting for a service on an unbundled service being provided on a long line is 4.2/6.4 = 0.66. When this weighting is applied to the 1.3% of lines in larger exchanges that the TERA model determines to be longer than 5km the correct proportion of unbundled lines longer than 5km is found to be 0.85%.

In summary, eircom finds that the ComReg weighting proposal is quite unsafe as it depends on the product of two numbers that are selected on a basis that has not been explained fully, other than by alluding to a precedent that similar numbers were used in France, and assumes that Ireland must be like France. If these numbers can be changed in an equally arbitrary way during any future review of LLU prices the proportion of eircom cost that will be recovered from LLU rental revenues will be subject to wild variation – and LLU pricing will be fundamentally unstable. Where data is available based on the experience of OAOs and eircom providing Broadband services in Ireland it has not been used to inform the weightings used in moving from the modelled cost to the prices proposed.

Option 4 for LLU

Q. 15. Do you agree that the charge at option 4 is the most appropriate charge for setting the LLU monthly rental charge going forward? Please state reasons for your response.

eircom does not agree that the charge at option 4 is the most appropriate charge for setting the LLU monthly rental charge going forward. If ComReg is to set a single national rate for LLU rental it must be based on a robust and stable treatment of the modelled costs. The selection of the two parameters used by ComReg to move from option 1 to option 4 is based on entirely arbitrary criteria. These parameters could be selected again at different levels in any future review of LLU price levels on the basis of "new" evidence that is no more compelling than the evidence presented here for the current values of 1,600 lines and 95% probability. In the absence of any compelling rationale for a robust mechanism to recover anything other than the nationally averaged cost per pair – and in the absence of any facility for eircom to recover the costs of above average costs from other wholesale access services – ComReg should set a single national price based on the entirety of the modelled network.

If ComReg proposes to set a single national price for LLU monthly rental it should be set on the basis of the weighted average cost of all loops currently providing service in Ireland. This is calculated at €16.52 per month as Option 1. If ComReg wishes to send a price signal to OAOs that there are lower cost loops available for unbundling in urban areas then more than one price should be offered. There are clear precedents for this approach in New Zealand and Finland. The Commerce Commission has recently set two prices for Telecom New Zealand local loops – a price close to €10.00 per month that reflects the lower cost of urban loops, and a price close to €25.00 per month that reflects the higher costs of rural loops. In Finland each incumbent local network provider has a distinct LLU price that reflects the unit cost of loops provided across their particular access network. Naturally both regimes encourage the unbundling of urban loops as the lower urban loop rentals reinforce the better scale effects available from unbundling loops at larger urban exchange sites. While these approaches reduce the likelihood of unbundling rural exchanges towards zero they have the benefit that they give predictability to both the incumbent and the OAOs that LLU prices are not set using the product of two parameters neither of which have a sound basis for selection, or any guarantee of future stability.

Option 2 for SLU

Q. 16. Do you agree that the charge at option 2 results in the most appropriate charge for setting the SLU monthly rental charge going forward? Please state the reasons for your response.

eircom does not agree that the charge at option 2 is the most appropriate charge for setting the SLU monthly rental going forward. If an OAO opts to locate equipment adjacent to eircom cabinets to unbundle sub loops they are more likely to achieve significant market share by targeting cabinets not connected to MDFs where OAOs currently unbundle full loops. Most urban exchanges currently have OAOs collocating to take full unbundled loops. It is unlikely that OAOs in that phase of investment can justify placing equipment close to eircom cabinets and stranding large elements of the MDF investment. In any case most urban exchanges are located within the cable franchise areas so penetration for the type of high-speed Broadband offerings that are required to justify a SLU investment will be reduced by cable competition.

Outside of the main urban centres many provincial towns actually present as promising candidates for a sub-loop investment. The absence of cable television networks leaves more room for both high-speed Broadband offerings and an IPTV service to gain sustainable levels of penetration. Many of these towns have eircom copper distribution networks that are highly "cabinetised" – and many are also the sites for Government MANs that can be used to provide fibre backhaul from the cabinet to the OAO head end with less investment than required in urban areas. In such areas characterised by potentially higher market share, more revenue streams, and lower levels of investment per cabinet, the OAO may well find that the economics for SLU investments look favourable for cabinets with less than 300 lines.

In summary, eircom finds the Option 2 selected by ComReg to be inappropriate for setting the SLU rental for two reasons. In the competitive environment in Ireland there is no evidence that urban areas present better economic prospects for achieving a return on a SLU investment than do provincial towns. Where local considerations indicate favourable economics for SLU investment, due to potential higher penetration of high-value services, the OAO may choose to unbundle cabinets with less than 300 lines.

<u>General Questions – Duration</u>

Q.17. Do you believe that given the current economic circumstances that a proposed price control period of three years with a review in year 2 is the most prudent option? Please state the reasons for your response.

eircom has two major areas of concern with ComReg's proposal for reviewing the model. Firstly, there is no mechanism for dealing with a sustained period of deflation or high inflation; and secondly, there is no provision for the eventuality that ComReg fails to replace this price control at the end of its three year life.

As ComReg has recognised, the current economic circumstances in Ireland make it very difficult to set an appropriate price control for the medium term. ComReg is proposing to set a price that is constant in nominal terms for three years, that is the price is not indexed to general inflation in any way. The ComReg model works in nominal terms, that is, there is no explicit treatment of inflation and the effect of inflation on returns over time is dealt with implicitly through the WACC used to annualise the capital costs. So long as inflation is a low positive number that is consistent with the WACC used in the model, using a constant nominal price for the control is internally consistent.

Unfortunately, inflation in Ireland is both very volatile and far from the ECB's target rate. Currently CPI is running at -4.7% (to May 2009) and is forecast to be -4.8% by the end of 2009. Given the economic instability in Ireland, it is entirely possible that there will be a sustained period of high inflation within the price control period. Any sustained period of either deflation or high inflation would render ComReg's fixed nominal price both inconsistent with the model and more importantly with general prices in Ireland.

Given the uncertainties regarding inflation over the period of the price control, eircom believes that it is essential that the final price control contains provisions that allow the price to be rapidly rebased in the event of significant deflation/inflation. [redacted]

Irrespective of when interim reviews of the price control occur, eircom is very concerned about the lack of clarity relating to what happens at the "end" of the price control period in the event that ComReg does not have a replacement control in place. The text of the decision instrument states the price directed shall apply "at any time thereafter". Were the directed price to remain in force after the end of the three year period, this would clearly be inconsistent with the recovery of the capital costs that ComReg has modelled. As set out above[redacted], the average line cost of €16.52 and the price for ULMP of €12.18 are both weighted averages of the modelled price for different years that make up the 3-year price control. The costs rise in each of these four years, and as explained in the overview above the cost per line will continue to rise exponentially over the life of the assets due to the positive tilts that ComReg have used to annualise the capital costs.

eircom has previously pointed out, during the course of our review of the model, that the weighted average price of €12.18 calculated from the model is calculated from (50%x2009 + 2010 + 2011 + 50%x2012)/3. This obviously pre-supposes a start date of 1st July 2009. If, as seems likely, the

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[redacted]

implementation date were to slip to 1st October 2009, the weightings would need to change to 25% 2009 and 75% 2012. This would have the effect of increase in the weighted average from €12.18 to [redacted]. Further slippage to 1st January 2010 would increase the figure to [redacted].

eircom proposes that, as part of the final Direction, ComReg should use the model to calculate the average charge that would apply from July 2012, either on an annually adjusted basis or as a fixed price for a second three-year priod, on the same basis as they derived the average for the first three years. eircom has attempted to perform this exercise, but it appears that the model is incapable of producing results for any year after 2013[4]. While the model cannot produce the required outputs, a simple linear extrapolation of the trend in the first four years suggests that, averaged over the second three-year period, the price of ULMP would be at least [redacted] per month. In the event that ComReg did not have a replacement price control in place at the end of the three-year period, this price for the average of the next three-year period would apply. In the event that, during three-year price control period, an interim review had amended the assumptions within the model, the price for the second thee-year period would be recalculated using the rebased model.

<u>General Questions</u>

Q. 18. Do you believe that the draft direction is clear, precise, and intelligible from a legal, technical and drafting perspective? Please state the reasons for your response.

Q. 19. Respondents are invited to comment on the draft direction from a legal, technical and drafting perspective as set out above.

eircom does not consider that the Draft Direction is sufficiently clear, precise and intelligible for the following reasons:

<u>The legal basis for the direction</u>

Reference is made in **section 1** of the Draft Direction to, among others "the SMP Decision", namely ComReg Decision D08/04. Having regard to the lapse of time since the market review that led to D08/04, ComReg is not entitled, in eircom's view, to review the price for LLU without first conducting and concluding a fresh market analysis. eircom refers to the position adopted by the European Commission with regard to Ofcom's notification of a proposed change to WLR. eircom notes that by referring in the Draft Direction to section 13 of D08/04 and Regulation 15(2) of the Access Regulations ComReg clearly suggests that it is amending eircom's obligation of cost orientation.

<u>References to the "Model"</u>

Section 2 of the Draft Direction include a definition of "Model" as follows: "*the costing model, developed by ComReg (in consultation with eircom) for the purpose of deriving the price of LLU and SLU, which has all necessary legal effect, including but not limited to the purpose of determining cost orientation and eircom's compliance with its obligation of cost orientation under section 9 of the SMP Decision*". Reference is then made to a Model so defined in **section 4** of the Draft Direction and **section 8.2.** In addition, **section 1.2** also provides that the Direction is made having regard to and having taken into account ... the Model".

[4] This deficiency is deeply troubling as the prices set for the first three years are only consistent with recovering the modelled costs to the degree that future prices rise to recover the costs of the deferred depreciation. If the model that ComReg uses internally has the same structural limitation as the one they have shared with eircom, it would appear that ComReg cannot have given any consideration to the prices in future periods that would be necessary to ensure cost recovery.

eircom believes that the definition is unclear. More importantly, eircom is of the view that the use of a reference to the "Model" to specify eircom's obligations of cost-orientation in the Draft Direction is inappropriate, superfluous and source of confusion.

First, there are several versions of the model in existence. In addition, the different models include parameters and functionalities which can be varied. Different *price* outputs result from these variations. As such, references to "costing" and "pricing" in the model are sources of confusion. (The costing model, in the version issued with 09/39, apparently gives an average cost of €16.52, but the Option 4 version of the ***pricing*** model calculates a price of €12.18.)

Moreover, the form of the Model and the choice of certain values for the parameters/functionalities concerned clearly amounts to decisions made by ComReg: this is the case of the use of a BU/LRIC methodology, the weighting of costs according to the length of lines and the size of exchanges, and the averaging over three years. The Model is simply a means for ComReg to translate these decisions in an LLU price, which ComReg considers to be cost-oriented. Reference should accordingly be made to ComReg's reasons for its choice for the model and the specific parameters rather than the Model.

In this respect, eircom does not accept, as the definition of Model and section 8 of the Draft Direction appear to suggest, that ComReg could vary - at its own discretion, and at any time - the values attributed to certain parameters/functionalities in the Model without having to explain the underlying reasons for it. It is irrelevant, contrary to what section 4.1 implies, that the price is calculated in accordance with the model. What matters is that the price reflects ComReg's decision and interpretation of eircom's obligation of cost-orientation (with which, for the avoidance of doubt, eircom entirely disagree), departure from which would require adequate justification and consultation. In other words, eircom does not accept that it could be open to ComReg, as the reference to the Model in section 8.2 suggests, to modify the parameters and impose a new LLU price on eircom as its whim provided, and justify such price on the basis that it is "derived from the Model". Such justification would be entirely insufficient and unacceptable.

For these reasons, eircom does not accept that the Model could have as such "legal effect". The expression "*which has all necessary legal effect, including but not limited to the purpose of determining cost orientation and eircom's compliance with its obligation of cost orientation under section 9 of the SMP Decision*" in the definition of Model is disconcerting. There should be no use of the "Model" for the purpose of defining the scope of eircom's obligation: in section 4.1, it would be sufficient to specify a price; similarly, eircom does not accept that it can be open to ComReg to amend the Model "at its sole discretion" as set out in draft section 8.2. and reference to the Model should be removed.

The directed LLU price

Section 4.1 directs eircom "*to charge no more than the following prices for LLU and SLU*" - with monthly amounts specified. It is not at all clear that the draft applies only to the recurring rental charge, and does not preclude existing, regulated, charges (such as those for survey, collocation facilities, connection (including GLUMP and ULMP), fault report, fault clearance and any other charges which may legitimately arise). eircom suggests that Section 4.1 makes it clear that it is only concerned with the monthly rental charge for LLU and SLU.

It would also be helpful if the Direction clarified whether, within this upper limit, rebate schemes and other types of discounts are allowed.

In addition, eircom believes that the geographic scope of application for the price should be clarified in the Direction, that is, that the directed price applies across the relevant market regardless of the exchanges being unbundled.

Revocation of ComReg Decision No. D15/04

Section 6.1 provides for the revocation of Decision D15/04 unless the Draft Direction, for one of the reasons specified, does not become effective. eircom notes that Decision D15/04 directed eircom to amend its prices on 1/12/04, 1/12/05, 1/12/06 and 1/12/07. This Direction has accordingly clearly exhausted its effects and there is no reason to revoke it or, for that matter, maintain it in force pending the entry into force of the draft Direction. (eircom notes that ComReg refused eircom's application to increase the LLU price in December 2008, in line with the precedent set in D15/04, on the basis that D15/04 no longer applied.) Section 6 appears to eircom for these reasons to be unnecessary and a source of confusion.

The review of the Draft Direction

ComReg has consulted on the period for which the price control should apply and proposes in Doc. 09/39 that it will apply for three years subject to review at year 2 unless exceptional circumstances warrant intervention prior to Year 2. However, this is not reflected in the Draft Direction: Section 4.2 of the Direction specifies that the Directed price will apply 30 days after the effective date, and at any time thereafter; section 8.1 provides that ComReg may at its sole discretion review and if it considers necessary amend, continue in place, replace or revoke the Direction. It is clear accordingly that contrary to ComReg's propositions in Doc. 09/39 the Draft Direction includes no sunset clause and would, in fact, remain in force forever unless amended or revoked. ComReg is awarding itself latitude that goes well beyond the findings of its Consultation.

eircom believes that this is entirely inappropriate and that the Direction should provide for the price control to apply for a period of three years, subject to a review at Year 2 and amendment if justified by exceptional circumstances.

eircom is also concerned with the absence of an end-date because the price control contains no provision allowing prices to be index-linked. In this instance, ComReg is relying on a model which has rising prices every year, but is setting a price control – with no end date – based on the average of the prices provided by the model over an initial three year period[5]. eircom notes that if the directed price were to continue in force beyond June 2012, the directed price would no longer be supported by the model.

ComReg should therefore explicitly end the price control at 30th June 2012, unless amended earlier.

Effective Date and implementation

eircom considers that the Draft Direction would not be capable of being implemented in its current form.

Firstly, eircom is entitled to appeal a Direction within a 28 calendar day period.

The draft determination suggests that the effective date will be the date of publication of the Decision notice (9.1). It further states that revised prices will be effective on all invoices issued 30 calendar days after the effective date (4.2). This is not reasonable or practical and fails to take into account the capability of eircom's current ordering and billing systems capability, or eircom's legitimate legal entitlements.

LLU is currently billed on a system called "Progressor". Each line is typically billed for discrete calendar months. In common with retail line rental and wholesale line rental, LLU rental is billed in advance. Invoices are issued between the 23rd and 27th of each month for the next month, i.e. rental for July will be invoiced in late June. However, while the invoice is issued late in the month, the charges are actually raised in the billing system at the start of the month, i.e. the rental charges for July are raised in the billing system on 1st June, and the invoices are printed and issued between 23rd - 27th June. This means that the price changes must be loaded into the billing system before the start of June to ensure that the charges raised on the July invoice – issued in late June – reflect the correct prices.

It is likely that a Direction giving rise to a price reduction may result in disputes between operators if the implementation obligation is unclear. In recent years, LLU prices increased with inflation. Any delay in implementing the change would mean the old, lower, price appearing on a bill for a future

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[5] In fact, the price ComReg proposes to direct is the one third of the sum of the prices in the model for 2010 and 2011, plus half the prices in 2009 and 2012: i.e. it properly applies only to a period from 1st July 2009 to 30th June 2012. This weighting will need to be amended as it is clear that the project will not be completed by 1st July 2009.

period: access seekers are not likely to complain in this case. In the present case, any delay would result in a higher price applying for a future period.

Based on the above, eircom believes that section 4.2 should be amended and provide for the application of any new price **60** days after the effective date. Such time would provide eircom with sufficient time to provide adequate notification to OAOs and implement the change in its billing system and avoid any unnecessary difficulties were eircom to exercise its right of appeal.

R.I.A.

Q.20. Respondents are requested to provide views (if any) which ComReg should consider in completing its Regulatory Impact Assessment.

In eircom's view, the question that should have been, and should be, addressed by ComReg in its Regulatory Impact Assessment (RIA) is: what is the appropriate form of price regulation of LLU, in particular the methodology for calculating the cost-oriented charge?[6] This is because the methodology proposed by ComReg, which diverges very significantly to the methodology adopted to date, has a very significant impact on stakeholders and relevant markets.

An RIA should serve to assist in justifying regulatory decisions which are likely to have material impact on stakeholders (including competition and consumers) by setting out and explaining why the decision taken was the most preferred option. It is not a bureaucratic add-on but lies at the heart of robust regulatory policy decision-making. Otherwise, decisions are prone to be arbitrary, opaque and wrong. The degree of complexity and sophistication of a RIA should be proportionate to the overall materiality of the Decision in question, which will, in turn, be largely governed by the likely extent and distribution of its impact on stakeholders (e.g. competition), as well as the availability of data for carrying out quantitative cost-benefit analysis. Whilst still heeding the proportionality principle, a clearly structured and complete RIA is necessary to ensure that decisions are soundly reasoned and evidence-based.

There is no doubt that a comprehensive RIA is required in the present case. eircom further notes that the conduction of a proper, thorough, RIA would not have constituted an onerous burden for ComReg in view of the relatively straightforward nature of the required analysis. ComReg's RIA, however, is given such cursory treatment that it does not meet the minimum requisite standard for an RIA appropriate to a decision of such significance on stakeholders and on relevant markets. This goes further than an error of process: an inadequate RIA carries the substantial risk that not all policy options will be explored and/or that the wrong policy will be selected. Put another way, a more comprehensive consideration of the impact of each of the options may have illuminated that a different option than the one chosen has the highest net benefits for consumers and society. ComReg's treatment of the RIA appears to reflect its erroneous belief that an RIA is not necessary for such a decision.

As explained in further detail below, eircom is concerned that ComReg's RIA reflects an analysis that is partial and narrow, which means it neglects consideration of important impacts on stakeholders, and competition more generally. The process deficiencies analysed below also serve to illustrate this fundamental issue. In Appendix 2, we provide a framework for what we believe would constitute an appropriate and proportionate RIA for this context.

Process Deficiencies

ComReg's RIA suffers from the following major deficiencies of form and process:

[6] Consideration of this question is made without prejudice to the prior questions of a) whether eircom has SMP, and, if it does, some form of regulation is a given and b) whether a cost oriented price control is the best form of regulation.

- The RIA has not adopted a correct structure, which makes it difficult to discern relevant impacts and the weighting applied to each of these;
- The relevant policy objectives, especially those specific to this context, are not sufficiently enunciated, which means it is unclear what ComReg is attempting to maximise in making its Decision;
- The analysis is partial, in that it focuses narrowly on the impact of reducing one price of one product in one market, without a holistic consideration of the wider impacts on a) other relevant prices and b) other relevant markets;
- Moreover, there is inadequate discussion of the appropriate weight that should be attached to the various costs and benefits experienced by each of the relevant stakeholders.

Substantive Deficiencies

ComReg's impact analysis is also substantively flawed because, in summary, it overlooks the centrality of the LLU price to date as a pricing input into other wholesale and retail products in the access network portfolio such as WLR, Line Share, retail line rental and bundling prices. More broadly, it fails to appreciate the interconnectedness of the price of, and demand for, LLU with other relevant wholesale and downstream markets. This is clear from the following observations:

- The RIA only considers two substantive alternative policy options, namely basing the charge on either

  (i) geographically averaged costs over all working lines or

  (ii) probability weighted costs, taking into account the probability of OAOs unbundling at certain exchanges, or lines of a certain maximum loop length.

  eircom's proposed format RIA in Appendix 2 considers a further policy option, namely where the geographically weighted LLU cost is charged to third parties but eircom is mandated to apply the geographically averaged cost as its imputed charge to itself. Identification and analysis of a third option enhances the robustness of the policy Decision;
- In assessing the rationale and impact of reducing the LLU charge from current levels, ComReg only focuses on the resultant increase in demand for LLU by OAOs. ComReg's assumption that a lower LLU price will increase LLU demand overlooks the interrelationship with, and critical role played by, relative prices of other alternatives such as WLR/Bitstream or Wireless/Cable;
- ComReg asserts that its preferred approach of basing the charge on the weighted cost of economic lines still allows for efficient cost recovery for eircom. However, ComReg is unclear whether the lower price for LLU applies to all WLR and retail lines. The consequences of each approach must be considered. As discussed elsewhere in the document, in the absence of a parallel consideration of how the cost of the uneconomic areas is to be funded, and in turn, the consequential impact of any measures to address this net cost, ComReg's proposed pricing approach is likely to seriously undermine efficient cost recovery. This will, in turn, compromise investment and innovation, with adverse impacts particularly experienced in rural areas, thus creating a digital divide, as discussed in response to question 11;
- In this regard, ComReg's proposed approach that LLU charges be based on the recovery of 'economic' exchanges and lines on the basis that OAOs should only contribute to the costs of the lines they purchase is specious reasoning, as it fails to recognise that that the largest effective purchaser of LLU is eircom, in its self-supply of LLU to itself in the provision of wholesale and retail broadband and telephony across Ireland. This logical flaw leads to the serious risk that eircom will be unable to recover the efficiently incurred costs of its national network.

These points are explored in more detail in the RIA framework provided in Appendix 2.

APPENDIX 1 –De-averaging

eircom absolutely rejects ComReg's proposal to set LLU prices based on a sub-set of large urban exchanges and refers ComReg to our response to ComReg Consultation 08/56 on this matter. Although eircom's position on the matter was explained in great detail in that response, it appears that ComReg has failed to adequately address any of the points made by eircom.

eircom is opposed to the setting of LLU prices on the basis of anything other than a national cost input. Below we address our reasons for opposing the geographical segmentation of the access market, the implications of geographical segmentation for USO funding and we analyse the determinants of the economic viability of an LLU exchange.

ComReg's Application of "Geographic" Approach to "Large" vs "Small" Exchanges

ComReg argues that it is less economic for an OAO to unbundle small exchanges, and that this justifies applying a lower weight to the cost of these exchanges in establishing a national weighted average cost. In order to apply this method ComReg requires two parameters:

- An assessment of what constitutes a small, uneconomic, exchange
- An assessment of the appropriate weighting to apply

In support of the definition of the boundary between large and small exchanges, ComReg cites, without references, OAOs in France and the UK as unlikely to unbundle exchanges with less than 1,600 and 2,500 lines respectively, and draws the conclusion that 1,600 lines is appropriate to the Irish context.

The cut-off at 1,600 lines would seem to be based on a number that will give a similar proportion of large and small exchange lines (68:32) as is observed in France – the only country where this form of weighting of "high density" and "low density" line costs has been used to set LLU prices. With 23% of the French population living in rural areas, as opposed to 39% of the Irish population, eircom expects that the smallest exchange that serves the highest density 68% of the French population is essentially urban in character, and very much larger than 1,600 lines. Nor does the selection of 1,600 lines as a "high probability/low probability" cut-off seem to reflect the experience of OAOs in selecting sites for unbundling in Ireland to date. [redacted]

ComReg does not deal explicitly with eircom's own use of copper pairs. If eircom were to separate its retail broadband organisation, one could consider it to have "unbundled" all sites where it has a DSLAM. In this case, many exchanges with less than 1,600 lines would be "unbundled".

We note that ComReg explicitly proposes to review the calculation regarding the 5km cut off for long lines (which we discuss below) but makes no reference to a review of the arbitrary 1,600 limit. It is not clear if it will be adjusted upwards if there are no sites of less than 3,000 lines unbundled, or adjusted downward if there are several sites of 1,000 or less unbundled. This could expose eircom and access seekers to unpredictable changes in price at some future time. If there is no clear basis for 1,600 lines as a cut off point, it could be changed to 3,000 lines, or 1,000 lines or even 500 lines in the future.

While eircom agrees that the number of working lines in a particular exchange area is a 'rule of thumb' indicator as to the economic viability of LLU, eircom does not agree that the pricing of LLU, which is a fundamentally important in terms of assessing investment choices and setting consumer prices, should be based on the simplistic application of such a 'rule of thumb'. Any operator considering LLU will examine a number of factors – not just the number of lines – in assessing the viability of LLU in any particular area. These include:

- The type and number of customers served from the exchange (e.g. a city centre exchange with a high number of lines may be limited to a small number of multi-line corporate and government customers that have limited demand for LLU delivered services using high capacity fibre delivered Broadband services instead).
- The demand from those customers for high speed Internet access

- The potential penetration of DSL-based broadband services. The presence of infrastructure competition in high-speed Internet access will limit the potential penetration of DSL. [redacted]
- The availability of transmission services for backhaul of LLU-delivered services to the OAO head end (ComReg acknowledges this factor is significant in section 5.6 of Consultation Paper 09/39).
- The availability of a government subvention to meet the once-off costs of locating the OAO equipment in the eircom exchange. The first OAO to avail of the eircom LLU offering unbundled loops in a number of provincial towns did so in a project that received government funding to encourage Broadband roll-out to rural areas. These exchanges are generally the smallest (measured by lines served) currently enabled for LLU, but all exceed 1,600 lines comfortably. On the other hand, it might be possible for a provider of National Broadband Services (with Government support) to unbundle very small sites.

eircom therefore does not believe that the number of working lines in an exchange, taken in isolation, is a good indicator as to the economic viability of an LLU investment. Even if the OAOs believe that the number of working lines at an exchange is a reliable indicator, there is no indication that 1,600 is the level that they have selected to determine viability. Furthermore, the economics of unbundling full loops and sub-loops are not sufficiently different that ComReg can rationally sustain a 1,600 line cut-off for the former and a 300 line cut-off for the latter. A suburban exchange less than 1,600 working lines with a high level of demand for Broadband services may have a better investment case for LLU than a larger city centre exchange with little DSL demand.

Having determined that all exchanges are large (>1,600) or small (<=1,600 lines) ComReg then applies a probability weighting to determine a price. The probability argument seems to be based on a test of the source of lines which ComReg would conduct after three years. If a random LLU line were chosen, ComReg assert it has a 95% probability of being from a large exchange, and 5% probability of being from a small exchange. In support of the weighting (95%:5%), ComReg cites, without specific reference, a 2002 ARCEP forecast of the take-up of LLU in France, and considers, based on interviews[7] with OAOs, that the French precedent is relevant to the Irish context because 'the proportion of high density exchanges/low density exchanges in Ireland is similar to that in France'[8][9] On the basis of this analysis, ComReg concludes that it is appropriate to apply a 95:5 ratio on the assumption that 5% of unbundled lines in Ireland will be in small exchange areas and 95% will be in large exchange areas. eircom does not believe that the validity of the assumptions underlying these weightings has been adequately checked by ComReg.

So, ComReg suggests that an exchange with 1,601 lines, with cable and wireless competition present, and no backhaul available, is 19 times more likely to be unbundled than an exchange with 1,598 lines, and cheap, government-subsidized backhaul available on a MAN. eircom does not agree this is the case.

If one considers eircom's own use of loops for broadband, then one might consider that eircom itself uses loops in exchanges with as little as 100 lines. eircom's analysis of the economics of DSL provision takes into account all the factors listed above: demand for DSL, presence of competition, availability and cost of backhaul.

In general, exchanges range from more viable to less viable. The most viable exchanges will be large, with short backhaul distance (i.e. urban), no viable alternative infrastructure operators and few other unbundlers present.

[7] Para 5.21, 5.22 'in the course of interviews with OAOs, they have **broadly** confirmed that they are less likely to unbundle small exchanges for economic reasons, **mainly** to do with the number of lines in each exchange

[8] Para 5.22

[9] eircom might note that ComReg appears to place unusual and largely unreferenced reliance on the characterisation of Ireland as being similar to France

The least viable exchanges will be those which are small, rural, and have no Bitstream participation.

Accordingly we do not believe that size, on its own, is an adequate proxy for the economic viability of LLU exchanges. We do not believe that ComReg should use exchange size as an arbitrary determinant of the geographic segmentation of the Broadband access market, as this approach will have serious consequences as outlined below.

Potential Deepening of "Digital Divide"

It appears that ComReg's proposals would create an incentive for eircom to invest in urban areas at the expense of rural areas, thus deepening any "digital divide" in the country. For example, if the LLU price is set on a national basis, eircom will be able to recover costs nationally and will thus invest across the country (what it might "lose" in the country it would be able to "recover" in the cities). However, if the LLU price is set based on a sub-set of cheap urban exchanges, eircom will be unable to recover the costs of rural investments. This effect will be exacerbated by the fact that eircom will be obliged to allow OAOs to rent loops from it at a price (of €12.18), which does not recover its legitimate costs. Furthermore, eircom does not believe that adequate USO funding will ever be available to it to make up the shortfall in funding and, in any event, ComReg has made it clear that would treat any USO funding submission with great care to ensure that only costs that were "avoidable" in absence of a USO would be claimable. The logical consequence of this scenario that eircom would concentrate to the maximum extent possible all Local Access infrastructure investment in urban areas, to the detriment of rural areas.

ComReg's Application of "Geographic" Approach to Long Lines

ComReg argues that it is not feasible to provide Broadband services over lines in excess of 5km in length. eircom notes, in this regard, that [redacted] of Broadband lines (wholesale and retail) are currently provided on lines in excess of 5km in length.

Absent any robust or reasoned analysis, ComReg asserts that the same weighting approach **and even the same weighting values** can be applied to long lines. There is no explanation of why a 5% weighting of long lines is appropriate and the application appears to eircom to be entirely arbitrary. If such a weighting were to be used at all, it should be grounded on evidence.

Analysis of the determinants of the economic viability of an LLU exchange

In general, exchanges range from more viable to less viable. The most viable exchanges will be large, with short backhaul distance (i.e. urban), no viable alternative infrastructure operators and few other unbundlers present.

The least viable exchanges will be those which are small, rural, and have no Bitstream participation.

Accordingly we do not believe that size, on its own, is an adequate proxy for the economic viability of LLU exchanges. We do not believe that ComReg should use exchange size as an arbitrary determinant of the geographic segmentation of the Broadband access market which will have serious consequences as outlined above.

Implications of geographical segmentation for USO funding

As ComReg acknowledges throughout the Consultation[10] there are many areas in Ireland in which it is not economic to provide access network services. Yet, eircom is obliged to provide such services wherever customers request service to be provided.[11] This Universal Service Obligation is central to the terms of eircom's Authorisation to operate telecoms services throughout the Ireland.[redacted]

Despite the universal nature of eircom's obligations in respect of access network services, ComReg does not believe this extends to the wholesale layer, and instead argues that it is not appropriate to calculate a nationally averaged cost per line in determining a cost oriented price for national full and sub-loop unbundled rental products.

ComReg contends that OAOs seek only to unbundle lines in order to provide Broadband services, and goes on to argue that because '*Unbundling exchanges takes time and is capital intensive*'[13],

[10] Multiple references, e.g. 09/39, Section 5.5
[11] Subject to €7,000 limit (Reasonable Access Threshold)
[redacted]
[13] 09/39, Section 5.6

OAOs will tend to focus their investment in exchanges where the greatest economies of scale can be found.

These arguments lead ComReg to argue that the cost of lines that are either uneconomic to unbundle (due to the low number of lines in the host exchange) or technically unfeasible to provide Broadband over (in the case of, for example, long lines) should be effectively excluded from the calculation.

Conclusion

ComReg's proposed weighted average methodology serves to highlight the inherent uneconomic nature of a significant proportion of eircom's national access network, but fails to take account of how the cost of that network should be recovered. This is in contrast to the situation in France, where we understand the issues of LLU price, and USO cost, were considered together.

The proposed methodology is flawed in logic and application, uses arbitrary and poorly referenced assumptions, and the implications of its implementation for the development of a competitive retail Broadband market in rural Ireland are extremely serious.

eircom cannot accept the principle of excluding any proportion of any subset of lines from the calculation of a nationally average price, *unless an explicit, credible and robust mechanism* is put in place to enable eircom to recover the cost of those lines excluded from the calculation for LLU pricing purposes. Absent such a mechanism, eircom rejects the principle and its application in the context of LLU pricing. ComReg proposes that a USO fund might be addressed at some point in the future, but absent such a mechanism, ComReg's proposals are simply not sustainable in the medium term.

To the extent that ComReg seeks to 'deaverage' prices by reducing prices in exchange areas likely to be unbundled to reflect costs in such areas but seeks to maintain the average price in higher costs areas, then it is axiomatic that a funding deficit will exist and that eircom, as the USO operator, is entitled to the benefit of a USO fund to ensure that it can earn its regulated rate of return. It is not acceptable that ComReg can seek to sidestep an issue of such significance by saying that it will consider any request for funding that may arise. It must openly acknowledge that a deficit will arise and set out how it will respond to the funding request which will inevitably follow including how it would propose to finance and guarantee the USO fund and address timing and payment issues. In the absence of a clear approach to such issues neither eircom, as the recipient of fund proceeds, or other operators (who may be required to contribute to the fund) can properly assess the merits of ComReg's proposed pricing approach.

The extracts below, from eircom's response to ComReg Consultation Paper 08/56, demonstrate eircom's absolute rejection of ComReg's proposal to set LLU prices based on a sub-set of large urban exchanges. Although eircom's position on the matter was explained in great detail in that response, it appears that ComReg has failed to adequately address any of the points made by eircom.

"eircom believes that this consultation [i.e. 08/56] is seriously flawed in both process and content. eircom is concerned that ComReg is seeking to construct an artificial 'price structure' to cater for the perceived demands of eircom's competitors rather than determining the most appropriate way to compensate eircom for use of its network and facilitate competition at a national level having objectively reviewed the conditions for competition on the national market for access services. The following errors in both process and content reflect eircom's concerns."

"No assessment of the impact of ComReg's proposals has been conducted especially on the recovery by eircom of its costs and the ensuing consequence in terms of eircom's current national pricing structure."

"The proposals under consultation are contrary to the central tenets of Government economic and social policy on balanced regional development and are also contrary to established regulatory policy and practice. They necessarily spell the end of geographically averaged pricing."

"...the consumer welfare impact of requiring eircom to compete with a wholesale service priced to recover levels of network cost below the national average has been either overlooked or ignored by ComReg in this Consultation Paper. The consequential impact on retail and wholesale prices for other services has not been assessed by ComReg in the Consultation Paper. This is a serious omission which will have major impacts on consumers, operators and on the market generally."

"The methodology proposed by ComReg is inadequate to determine a cost-oriented price for LLU on the national market for local access and can only be explained by the desire to achieve an artificially low price for LLU. It would appear from ComReg's preliminary finding in the WUA Consultation that the WUA market is national that ComReg is of the view that the conditions for competition are similar across Ireland and that competition would benefit from the provision by eircom of access at cost-oriented price to unbundled loops in the entire geographic market defined on a national basis. This cannot be reconciled with ComReg's proposed methodology excluding certain areas on the basis of whether or not competition exists and/or will develop. A price which does not allow eircom to recover the national average cost of the local access network cannot be considered to be cost-oriented and constitute an inadequate and inefficient price which will result in encouraging LLU in areas already marked by infrastructure-based competition, while removing any incentives for operators to move to those rural areas considered by ComReg to be "unlikely to be unbundled"."

"eircom fundamentally disagrees with ComReg's proposal that "because OAOs are unlikely to unbundle 100% of exchanges, the price of LLU should reflect only the cost of those lines that are likely to be unbundled over the timeframe of this review" and rejects any suggestion that eircom's current LLU prices .... are not cost-oriented. ... eircom believes that ComReg's proposals will lead to an under recovery of costs by eircom on a national basis which ComReg appears to have entirely ignored."

"eircom strongly opposes ComReg's proposal to set LLU prices on the basis of only part of the costs incurred by eircom in relation to its access network. eircom believes that ComReg's proposal is at odds with the principle of cost-orientation and is entirely inconsistent with eircom's current obligation of access which applies across all of its local network over Ireland, and with ComReg's proposal in the WUA consultation, to continue to define a single national relevant market for unbundled access. eircom submits that ComReg's proposals will not result in a cost-oriented price for LLU because it will not allow eircom to recover the legitimate costs associated with its national local access network."

"eircom further notes that ComReg has not indicated any of the means by which it would propose to determine whether a line is likely to be unbundled or not. eircom believes that such an assessment is to a large extent subjective and operator dependent. eircom is concerned in this regard that ComReg's proposals reflect a desire to predetermine or contrive a specific outcome."

"eircom submits that ComReg's proposal will inevitably lead to the geographic de-averaging of retail tariffs with adverse consequences on the affordability of services in rural and high cost areas and for socially vulnerable groups. This is contrary to clear Government policy on national economic development where specifically through the National Spatial Strategy initiative, industrial, social and economic expansion will be attracted away from the current major areas of concentration, in particular the Dublin region. It is also contrary to ComReg's own objectives".

APPENDIX 2: Proposed RIA framework for ComReg LLU decision

Introduction

As discussed in the body of this document (response to q. 20), ComReg's RIA is profoundly deficient, in process, style and substance, such that it has not met the minimum requisite standard for an RIA appropriate to a decision of such significance on stakeholders and on relevant markets. This not only amounts to an error of process, but an inadequate RIA carries the substantial risk that not all policy options will be explored and/or that the wrong policy will be selected.

Regulatory decisions which are likely to have material impact on stakeholders, competition and consumers should be justified by an RIA, which sets out and explains why the decision taken was the most preferred option. An RIA is not a bureaucratic add-on but lies at the heart of robust regulatory policy decision-making; otherwise, decisions are prone to be arbitrary, opaque and, worse, wrong. The degree of complexity and sophistication of an RIA should be proportionate to the overall materiality of the decision in question, which will, in turn, be largely governed by the likely extent and distribution of its impact on stakeholders and competition, as well as the likely availability of data for carrying out quantitative cost-benefit analysis. Whilst still heeding the proportionality principle, a clearly structured and complete RIA is necessary to ensure that decisions are soundly reasoned and evidence-based.

The question to address in this context, within a properly constructed RIA, is: what is the appropriate form of price regulation of LLU, in particular the methodology for calculating the cost-oriented charge?[14]

The basic objective of an RIA is to inform policy choice and ensure that the chosen policy is robust and leads to the choice of the most preferred policy – one with the highest net benefits - out of a range of alternatives, given relevant policy objectives.

An RIA should therefore generally be structured along the following lines:

- **Background; define the issue and general consumer interest**: this initial section of an RIA should be a brief summation at the outset of the relevant background, essentially addressing the question of what is motivating an RIA to be performed and what is the associated consumer interest.
- **Articulation of policy objectives and (relevant) regulatory principles**: Before the selection and comparative analysis of policy options, it is first necessary to enunciate the relevant policy objectives. In the absence of this consideration, the selection of the policy choice will be arbitrary and at risk of not promoting relevant regulatory objectives.
- **Identification and description of policy options**: The purpose of this section is to identify and describe a range of policy options, out of which a preferred option will emerge from an analysis and evaluation of the direct and indirect impacts (costs and benefits) of each of the options.
- **Impacts on stakeholders, in terms of costs and benefits of each of the options**: Following an identification of relevant stakeholders, this section looks at the impacts of each of these options on these stakeholders.

[14] Consideration of this question is made without prejudice to the prior questions of a) whether eircom has SMP, and if it does, some form of regulation is a given and b) whether a cost oriented price control is the best form of regulation.

- **Impact on competition:** Given the centrality of competition to a regulator's remit, this section assesses the impact on competition of the proposed measures
- **Risks and unintended consequences** of each of the options: this section contains some exploration of whether the purported benefits or costs of the options carry any particular risks/variance, or whether unintended consequences may follow
- **Assessment and selection of most preferred option:** this section of an RIA concludes on the most preferred policy option, in light of the identified impacts on stakeholders and competition,

This Appendix provides a framework for an RIA suitable to this context, and is organised below in accordance with the above structure.

Define the issue and general consumer interest

The issue which this RIA addresses is the appropriate methodology to calculate cost/charge for LLU, given ComReg's policy objectives. In particular, ComReg's proposal to change the methodology used to calculate the LLU charge entails changes to the resultant price of LLU, with consequent impacts on other products for which LLU is an input. This prospect has potentially far-reaching implications for stakeholders, (including competition and ultimately consumers), which are explored below in this document. It also carries distributional issues, i.e. where net benefits of options might be similar, it may be appropriate to consider impact on different groups, e.g., urban vs. rural customers, more vs. less advantaged.

Thus, the basic driver of this RIA is that the direct and indirect impacts on stakeholders, competition, investment incentives, and efficiency of changing the LLU price needs to be thoroughly considered before deciding on the preferred policy option.

Policy objectives

The basic question considered in this section is: what is ComReg seeking to maximise in making its decision?

In this regard, it will be necessary to consider relevant legislative objectives, regulatory principles, and specific policy objectives.

Relevant legislative objectives

The following sections of the Act[15] appear most relevant to this context:

12.—(1) The objectives of the Commission in exercising its functions shall be as follows—

(a) in relation to the provision of electronic communications networks, electronic communications services and associated facilities—

(i) to promote competition,

(iii) to promote the interests of users within the Community,

(2) (a) in so far as the promotion of competition is concerned—

(i) ensuring that users, including disabled users, derive maximum benefit in terms of choice, price and quality,

(ii) ensuring that there is no distortion or restriction of competition in the electronic communications sector,

(iii) encouraging efficient investment in infrastructure and promoting innovation.

(c) in so far as promotion of the interests of users within the Community is concerned—

(i) ensuring that all users have access to a universal service

In essence, therefore, the relevant policy objectives that ComReg should seek to maximise in making the choice of which LLU pricing methodology to adopt are the promotion of competition, ensuring that no anti-competitive conduct occurs, encouraging efficient investment, and ensuring universal access to services.

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15 http://www.irishstatutebook.ie/2002/en/act/pub/0020/sec0012.html#partii-sec12

Regulatory principles

In making decisions, it is incumbent upon ComReg to adhere to its stated regulated regulatory principles[16] of:

- Necessity
- Effectiveness
- Proportionality
- Transparency
- Accountability
- Consistency

The particular relevance of each of these principles is highlighted in the context of the impact analysis of each of the options below.

Specific objectives

In addition to the broad legislative policy objectives, this section considers the relevant policy objectives specific to the context of regulated pricing of LLU. The objectives of most relevance include:

Promotion of competition in broadband and telephony markets;

Encouragement of efficient investment in these markets; and,

Facilitation of broadband services for all citizens, regardless of where they live.

Note in this regard that the objectives of promoting LLU take-up and broadband penetration may be better seen as intermediate/secondary objectives or as by-products to the overarching ones above.

It may also be appropriate to transparently apply some weighing to these objectives, given that these may conflict in the impact analysis.

Identification and description of policy options

This section identifies and describes a range of policy options, out of which a preferred option will emerge from the analysis and evaluation of the direct and indirect impacts (costs and benefits) of each of the options. The policy options considered below represent the various modelling approaches to the calculation of LLU charges. The subsequent analysis proceeds by comparing the incremental costs and benefits of adopting new alternative options relative to the option of 'doing nothing', i.e. where the current methodology was rolled forward. Hence the first option, against which other options are compared, is the 'do nothing' option of continuing to adopt the previous methodology.

The focus of this RIA should be on the choice of methodology for calculating LLU charges; the choice of which model to which any methodology is applied is a separate and prior question. The comparison of the old model vs. the new model raises its own issues; however eircom agrees that the new model is a more sophisticated model of eircom's access network. Thus, for the purposes of this RIA, it is assumed that the new model will be used for the computation of LLU charges. The options to consider are therefore around the different methodologies which could be applied to the new BU-LRIC in order to generate LLU charges and about the resultant structure of prices that the methods generate.

Option 1: Do nothing: new model, average cost per line based on all lines

This policy option is to continue to apply the methodology as was applied to the previous model. That is, the charge is based on the cost of the entire access network, taking into account all working lines, i.e. the charge represents the average cost of all lines. As discussed, this option represents the counterfactual against which the alternative options are compared in terms of incremental impacts (benefits and costs) on stakeholders, including competition. It should also be noted that the relevant

[16] Set out in http://www.betterregulation.ie/eng/Government_White_Paper_'Regulating_Better'/RegulatingBetterGovernmentWhitePaper1.pdf

counterfactual is how the market would have developed in the foreseeable future had ComReg adopted a continuation of policy. That is, the alternative options are not compared to the world *today*, but rather to the world as it would have developed had ComReg not changed its approach.

Option 2: new model, OAOs and eircom avail of weighted average cost per line

This option is broadly described in ComReg's consultation. The key aspect of this option is that it implies that the LLU price will be below the average cost of a line in many areas of the country, mainly rural areas. The refinement in the articulation of this option is that, in addition to it being the explicit LLU charge to third parties, the resultant calculated charge would also then be used as the imputed price in the cost stack of eircom wholesale and retail products to which LLU is an input.

In particular, this option would allow eircom to impute the resultant LLU charge in the following products:

- WLR
- Retail line rental
- Retail (stand-alone) broadband
- Retail bundled products (multi-play)

Option 3: As Option 2, but differential charges applied to OAOs and eircom portfolio

Option 3 is the application of the same methodology as option 2 to calculate the per line LLU cost, which would remain as the charge for LLU supply to third parties. However, in terms of eircom's supply of LLU to itself in the case of dependent products, eircom would be mandated to use the calculated geographically averaged cost arising from option 1 as the imputed charge.

Impacts on stakeholders

Following an identification of relevant stakeholders, this section looks at the impacts of each of these options on these stakeholders. The next section then looks at the impact of the proposals on competition. These impacts are considered primarily qualitatively. Also outlined is the quantitative analysis that could be performed. One general theme running through this impact assessment is the centrality and interconnectedness of LLU with other products in broadband and telephony markets.

Identification of stakeholders

These constitute the range of stakeholders most likely to be positively or adversely impacted by the choice of policy:

- eircom
- OAOs
- Competing access infrastructure (cable operators, FWA, and mobile broadband Operators)
- Consumers, within which further distinction is made between:
  - urban/rural, and, where relevant,
  - within cable footprint/outside cable footprint.

Option 1: Do nothing: new model, national average

As discussed, this option is the counterfactual against which the incremental costs and benefits of the alternatives are assessed. Therefore, it is not necessary to discuss the benefits and costs of this option in absolute terms. Rather, the advantages and disadvantages of this option emerge in the context of assessing these incremental costs and benefits. As discussed, this option is the world how it would develop under a continuation of ComReg's approach to LLU pricing. In this regard, the prevailing trends in competition appear to be a re-emergence of cable operators in the market, as well as greater fixed-mobile substitution. Therefore, competition in relevant markets is likely to improve going forward even under no change to ComReg policy.

Option 2: new model, OAOs and eircom avail of weighted average rate

Impact on eircom

This sub-section considers the incremental impact on eircom from a policy change from the current charging methodology to the adoption of option 2 as described above, taking into account the resultant changes to, and the impact of, the vertical structure of prices.

The practical manifestation of this option is that, due to the suppression of the cost impact of 'uneconomic' lines on the cost base, the resultant LLU charge will fall significantly from current levels. For example, based on ComReg's choice of inputs, the LLU charge falls from €16.43 to €12.18. This can be expected to have a range of impacts on eircom.

At face value, it could be expected that demand for LLU would rise. The extent of this increase will be determined, inter alia, by the price elasticity of demand for LLU by OAOs, and the resulting vertical structure of prices and its impact on operator decisions. The increase in demand for LLU will be mitigated to the extent that the elasticity of demand for LLU is low (in absolute value) and where it is expected that alternative infrastructure (cable) operators will become more competitive. Thus, on the one hand, this option could be expected to increase the quantity of LLU sold and associated revenues, thus yielding increased wholesale revenues for eircom.

- On the other hand, this expected increase in LLU take-up would be likely to lead to an increase in competition in retail broadband markets in urban areas. From a revenue and market share perspective, this could be adverse to eircom. That said, this effect can be seen as a benefit of competition facilitated by regulation.
- The above effect on LLU demand is, however, only a partial effect of the move to Option 2. The change in methodology will also have important impacts on related retail price levels and structures as between urban and rural areas and associated impacts on market size and structure. In response to a reduction (below what would have occurred in the counterfactual) in both the explicit and the imputed LLU price, eircom will effectively be supplying lines in urban areas – either LLU, WLR or retail lines – at a price closer to or at the cost of production of lines in urban areas. This significantly reduces any margin that would have been earned on the provision of these lines under the continuance of ComReg's current approach to LLU pricing. In parallel, under a national pricing policy, the price in rural areas will fall further below the cost of production in those areas. This highlights both the loss made in providing rural lines, and, to the extent that eircom supplies the rural market below cost, also crystallises these losses. The move to option 2 thus has the effect of removing the ability of eircom to cross-subsidise rural lines with revenues from sales in urban areas. In the absence of a funding mechanism such as a USO fund, this would undermine eircom's ability to recover the costs of its access network. This, in turn, would undermine efficient investment in eircom's access network.

A further impact derives from the ability to impute this charge in pricing of dependent products. This provides eircom with the flexibility to reduce the charge on these products, particularly on retail broadband and, where WLR charge is calculated on a cost+ basis, the price of both WLR and retail line rental.

Box 5.1: Quantitative analysis of impact on eircom of Option 2

The above discussion has highlighted some qualitative impacts on eircom of the reduction in price of LLU from €16.43 to €12.18 per month. These impacts can be quantified as follows: The increase in demand for LLU by OAOs can be modelled by estimating the demand function, based on elasticity estimates. The demand function is a derived demand and would be a function of the retail demand for broadband, final retail price, and price of substitute products such as WLR and Bitstream. This would potentially yield an estimate of the resultant change (increase) in LLU take-up.

The €4.25 reduction in the explicit and imputed charge for LLU will also give rise to an important revenue loss for eircom. [redacted] This lost revenue also removes the ability to cross-subsidise from urban to rural customers under a national pricing policy. Quantitative analysis could illuminate the likely losses made on provision of lines in rural areas under the move to an LLU price of €12.18.

The impact on take-up of WLR and Bitstream would also be quantified, due to the change in relative attractiveness of LLU vs. WLR and Bitstream.

Impact on OAOs

A move to a weighted average charge methodology and the associated significant reduction in LLU charges would likely translate to a material increase in demand for LLU by OAOs, from its current levels. The price reduction would enhance the economics of unbundling, effectively extending the set of exchanges at which LLU is economically viable, and enable OAOs to better differentiate their services than is the case with a reliance on WLR and/or Bitstream.

Box 5.2 Quantitative analysis of impact on OAOs of Option 2

These impacts could be estimated quantitatively by modelling the decisions faced by OAOs with respect to unbundling, given the LLU charge, the other costs of unbundling, the density of the exchange, and the price of substitutes. The impact on take-up of WLR and Bitstream would also be quantified, due to the change in relative attractiveness of LLU vs. WLR and Bitstream. Likely retail pricing strategies of OAOs could also be modelled.

Impact on alternative access providers

The heightened competition in urban areas would, in the short term, adversely impact on cable, mobile broadband and FWA operators. Indeed, at a certain price point, ULMP pricing could render some operators' remaining planned investment uneconomic. However, against that, the force of competition could also induce greater product differentiation and innovation.

Box 5.3 Quantitative analysis of impact on alternative access providers of Option 2

The impact on alternative operators could be estimated by the effect of the reduction in price on their margins. In addition, it would be assumed that some lines would be lost to OAOs taking LLU. The net impact is likely to be a fall in profitability and a loss of market share. The long term impact on competition is considered in the section on competition below.

Impact on consumers

This is likely to be positive in the short term, as LLU charge reductions feed through into lower prices for retail broadband and/or bundles, with attendant increases in broadband penetration in urban areas.

As discussed, consumers in urban areas are likely to benefit from lower prices and heightened competition. However, there will also be a distributional aspect to the consumer impact, as urban consumers will fare differently to those in rural areas. The latter are likely to be adversely impacted under the proposed remedy (in the absence of funding), as they are significantly less likely to benefit from competition provided by un-bundlers, who will focus their roll out on more economic urban areas.

Moreover, as discussed above, eircom's investment incentives will be undermined under this option, which will be primarily manifested in reduced focus on uneconomic areas. The adverse effects of this option on rural consumers will be particularly acute where a lack of fixed broadband is provided. The net effect to highlight is a situation where availability, choice and prices are different in urban and rural areas.

Box 5.4 Quantitative analysis of impact on consumers of Option 2

As discussed, the direct impact on consumers would be different as between urban and rural customers. The impact on urban customers would be a function of the reduction in retail prices resulting from the LLU charge decrease and the increase in broadband demand. Rural consumers would, by contrast, experience a reduction in the overall availability and choice of broadband.

Option 3: new model, OAOs avail of weighted average rate, eircom of national average

Impact on eircom

Were eircom mandated to use the geographically averaged rate as the imputed price in its cost stack, this would have a significant impact on relative prices of LLU and products for which LLU is an input, such as WLR, retail line rental and retail broadband. In particular, the price of WLR and eircom retail line rental would need to reflect the national average cost of a line, whereas OAO products would be built on the explicit LLU charge. Such a price structure would mean that eircom's prices would be significantly above those offered by OAOs in urban areas. Further, by preventing eircom from reducing its retail prices, eircom is also exposed to competition from cable, which has urban-only footprint. This would potentially render eircom uncompetitive with OAOs and alternative access providers in downstream telephony and broadband markets.

At the same time, it would also further hamper eircom's ability to serve rural broadband customers, due to the loss of customers and profits in urban areas. Moreover, eircom's inability to lower its prices in rural areas would, over the period of this review, serve to constrain its ability to compete with mobile operators in rural areas in the provision of both voice and data. As compared with option 2, this option could therefore be more adverse to eircom.

Box 5.5: Quantitative analysis of impact on eircom of Option 3

This would extend upon the analysis performed for the impact of option 2. The main difference would be modelling a greater loss of lines to unbundling OAOs in urban areas. The impact on take-up of WLR and Bitstream would also be quantified, due to the change in relative prices as between LLU, WLR and Bitstream.

Impact on OAOs

This option has an even more significant positive impact on OAOs than was the case under option 2, as OAOs will be able to aggressively compete with alternative network providers in urban areas, whereas eircom will be forced to maintain a price structure based on the nationally averaged cost of a line, rendering eircom uncompetitive with both OAOs and alternative access providers.

Box 5.5: Quantitative analysis of impact on OAOs of Option 3

This would be a further application of the analysis under option 2, with a greater take-up of LLU, due to the inability of eircom to reduce the prices of products for which LLU is an input. This would again be modelled using a demand and supply model of LLU and broadband demand. The impact on take-up of WLR and Bitstream would also be quantified, due to the change in relative prices as between LLU, WLR and Bitstream.

Impact on alternative access providers

The impact on alternative access providers such as cable operators is similar to that identified under option 2 in that they face more competitive pricing from their competitors. . In this case, however, the main source of increased competition is OAOs, rather than eircom. This is because OAOs are able to avail themselves of the cheaper LU price whereas eircom is constrained to price at a level reflecting nationally averaged prices, and hence is forced to maintain an uncompetitive price point. In rural areas, however, mobile operators would be better placed than under Option 2 to compete with eircom in the provision of voice and data to rural consumers.

Box 5.6: Quantitative analysis of impact on alternative access providers of Option 3

Modelling could quantitatively estimate the loss experienced by alternative access providers such as cable operators, in terms of lines lost, market shares, and profitability. It could also illuminate the competition that would take place between eircom and mobile operators in rural areas.

Impact on consumers

Consumers in urban areas may face price decreases led by reductions in price (beyond those that would occur going forward under the counterfactual) of retail telephony and broadband services offered by OAOs taking LLU at the reduced price. However, those consumers who continue to use eircom's retail services will not enjoy such price decreases due to the price floor faced by eircom, as discussed.

The nature of the impact on consumers in rural areas would depend on the extent to which eircom is able to continue to cross-subsidise these consumers from revenues earned in urban areas. It is most likely the case that eircom will be significantly constrained in doing so, due to loss of lines in urban areas to OAOs and to cable. In the short term, consumers in rural areas are therefore worse off than under Option 2, since prices are forced to be maintained at the higher level based on nationally averaged costs.

Box 5.7: Quantitative analysis of impact on consumers of Option 3

This analysis would quantify the effects described qualitatively above. In particular, modelling could illuminate the extent of eircom's loss of lines in urban areas and the consequent impact on investment in rural areas.

Impacts on competition

Option 1: Do nothing: new model, national average

Competition under option 1 is assumed to develop in the direction it would have taken were ComReg to uphold its current approach to LLU pricing. In this regard, it should be noted that, whilst LLU take-up is not high in Ireland, this does not necessarily imply an uncompetitive market or one characterised by a lack of innovation. It should be recognised that LLU take up is a means to an end, namely healthy competition in retail broadband. In addition, the presence and increased potency of cable operators in urban areas, as well as the national presence of mobile broadband, should also be taken into account when assessing the likely future state of competition in broadband in Ireland.

Option 2: new model, OAOs and eircom avail of weighted average rate

Notwithstanding the above, this option is likely to further promote competition in broadband, with associated benefits in terms of lower prices, better quality and choice. Further, the nature of competition facilitated by LLU rather than bitstream is typically more sustainable and one that gives rise to greater service differentiation.

- This option is also likely to have a significant impact on the size and structure of the retail broadband market. The biggest driver of take up of LLU is likely to be the migration of existing WLR/Bitstream lines. However, to the degree that there is a net increase in the take up of copper lines on the eircom network, this will substantially be at the expense of other platforms.

- Thus the net impact on competition under this option is indeterminate, and would depend on the extent to which the increase in competition provided by uptake of LLU is offset by the impact on alternative access providers' margins on their ability to provide a source of sustainable competition.

Box 5.8: Quantitative analysis of impact on competition of Option 2

Quantitative analysis could be carried out to consider the impact on the size of the market, broadband penetration and market shares, distinguishing between the urban and retail markets. The way in which this could be conducted could involve constructing a model of the current broadband market, showing current retail market shares. Scenarios could then be run showing how the market would have developed under the continuance of option 1 versus its development under lower LLU price and under different assumptions regarding take-up, demand elasticity, and churn over time. Due to LLU being an input into WLR and ultimately retail line rental, it would also be necessary to conduct analysis of the impact of a reduction in the LLU price on price and take-up of WLR and retail line rental, and resultant market shares.

Quantification of consumer benefits from competition in form of increased consumer welfare from reduced price and increased take up could be carried out. This could involve constructing a model of the market and assessing the increase in consumer surplus under a given demand function.

Whilst the benefits of this option are relatively clear and demonstrable in the form of increased competition in retail broadband in urban areas and associated consumer benefits, the costs in the form of the removal of the subsidy to consumers in rural areas must also be considered. There are three main ways the net cost of uneconomic areas can be funded:

- By cross-subsidising of rural areas by urban customers, as under option 1
- By eircom shareholders
- By an explicit USO fund.

In comparison to option 1, the likely outcome would be a transition from a single retail broadband market to separate geographic markets. However, due to the loss made on the provision of rural lines, eircom would also require compensation in the form of a USO or similar in order to serve uneconomic rural areas.

Each of these types of funding gives rise to their own costs, which must also be taken into account in the assessment of this option. For example, a USO surcharge will increase the prices of all telecoms services, leading to some pricing distortion.

Thus the merits of this option turn on a trade-off of these competition and consumer benefits against the costs arising from the removal of the subsidy to rural areas.

Option 3: As Option 2, but differential charges applied to OAOs and eircom portfolio

On the one hand, competition in the short term under this option is likely to be strengthened, since it facilitates greater take up of LLU. However, judged holistically, these benefits would be offset by the significant distortion to competition that arises from a situation where eircom and OAOs compete facing different factor input prices. The obligation on eircom to charge itself the national average per line cost whilst OAOs avail the lower weighted cost would not be competition on the merits. In particular, eircom would not be able to compete with OAOs at the retail level, since it would be constrained from reducing its prices in order to pass an imputation test. Furthermore, as discussed, this option would allow greater scope than is the case under option 2 for mobile operators to compete for customers in rural areas. This would further erode eircom's ability and incentive to serve and invest in rural areas. .

These costs would have to be weighed up against the competition benefits arising from this option. 2

Box 5.8: Quantitative analysis of impact on competition of Option 3

Quantification of the costs and benefits to competition would proceed as shown above for Option 2. The main difference to bring out in the modelling of Option 3 is the distortion of competition arising from the different cost bases of OAOs and eircom. Quantitative modelling could be also carried out to demonstrate the development of the market into an urban /rural split, with very different competition conditions.

Risks and unintended consequences

This section considers both the risks and the potential unintended consequences of each of the policy options, in particular whether the purported benefits or costs of the options carry any particular risks/variance, or whether unintended consequences may arise. Such analysis can complement the impact analysis above in terms of cautioning the selection of the policy with the highest net benefits to the extent that these net benefits are subject to particular risk and/or the policy apt to give rise to unintended consequences.

The framework in which risk is considered below is a Type I/Type II error framework. This looks at whether there are any systematic biases in the risks of the options, e.g. where the risk of too low a price [regulating too much – Type I error] are greater than with too high a price [not regulating enough – Type II error].

Option 1: Do nothing: new model, national average

The main risk of maintaining the current approach is that LLU is not encouraged where it may be the key stimulus to broadband competition. The unintended consequence of such an option is therefore that the pursuing such a policy could carry the risk of dampened increases in broadband penetration, with consequent opportunity losses for Ireland's competitiveness.

Option 2: new model, OAOs and eircom avail of weighted average rate

The principal risk with option 2 is that the increase in LLU take-up in urban areas does not materialise, whilst at the same time, the ability to subsidise rural areas is undermined due to reductions in retail prices brought about, inter alia, by the concomitant fall in the WLR charge. Another risk is that it undermines the viability of the cable operators, which are important sources of sustainable competition.

In the framework of Type I/II errors, it could be argued that the risk of not sufficiently reducing the price is more than that of reducing the price too far. However, this is predicated on some form of USO funding being committed in order to compensate eircom for the losses it will incur on a large proportion of lines.

Option 3: As Option 2, but differential charges applied to OAOs and eircom portfolio

Option 3 is characterised by similar risks to option 2. A further risk, however, is that the urban/rural digital divide is widened under this option, due to eircom's reduced ability to effectively serve rural customers. It is also possible that OAOs will not reduce their retail prices but rather retain the increased margin for themselves, which would mean urban consumers would not be positively affected through lower prices under this option.

Evaluation of most preferred option

In light of the range of impacts on stakeholders and competition identified above, this section brings together these findings and makes an assessment of which option is most preferred.

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2 Vodafone Ireland Ltd.

Vodafone Response to the ComReg Further Consultation on Local Loop Unbundling and Sub Loop Unbundling Monthly Rental Charges

Ref. ComReg Document 09/39 Response Date: 12 June 2009

Introduction

Vodafone welcomes the opportunity to respond to this further ComReg consultation on Local Loop Unbundling and Sub Loop Unbundling Monthly Rental Charges. The recognition by ComReg in the consultation document of the need to encourage sustainable competition and efficient investment in the fixed line sector through enabling access to LLU and SLU at competitive prices is especially welcome, and a position that Vodafone strongly supports.

While we share ComReg's view that a new BU-LRAIC modelling approach is required at this stage to ensure that eircom is fully compliant with its obligation of cost orientation in the prices charged to competing operators for LLU and SLU access, Vodafone differs with ComReg on many aspects of the details of the proposed modelling approach and believes in particular that the proposed price of €12.18 per line for LLU monthly rental remains considerably above the level consistent with the underlying efficient costs to eircom of LLU access provision. Vodafone contends that the changes to ComReg's proposed modelling approach set out and justified in this consultation submission must be adopted by ComReg in deriving the final regulated access charge for LLU monthly rental for the time period of the review. These changes, if implemented, will ensure that optimal LLU and SLU prices are set that will facilitate innovation, efficient investment, and enhanced competition in the provision of fixed line broadband and other communications services. The revision of ComReg's current modelling approach based on the recommendations set out by Vodafone will therefore be to the ultimate long term benefit of end users in the form of lower prices and greater quality and choice in the communications services that they consume. ComReg must not allow the current exceptional opportunity to promote competition and investment in the fixed line sector to be missed through the setting of inefficiently high LLU and SLU access charges.

Our detailed position on the particular issues addressed by ComReg in the consultation document is set out in full in subsequent sections and in response to the consultation questions below.

Level of Disclosure of Information

Vodafone is concerned by the very limited level of disclosure in the consultation of costing and other information that was central to the calculation of the current proposed LLU per line monthly access charge of €12.18. We acknowledge that given the confidential nature of much of this information, full transparency cannot be provided by ComReg on these costs. Nonetheless the lack of information seriously limits the capacity for Vodafone and other interested parties to provide informed comment on the proposed costing approach. Vodafone notes that the level of disclosure of relevant information by ComReg in this consultation process falls significantly short of that provided by NRAs in other countries in the process of determining LLU and SLU access charges in their jurisdictions. In particular, Vodafone would refer ComReg to the extensive information made publicly available by Ofcom in its recent review of the charge controls for unbundled local loops and other services provided by BT Openreach. We would therefore urge ComReg to consider whether additional information can be provided to provide greater transparency to respondents on the inputs forming the basis for the current proposed LLU and SLU charges while still addressing legitimate confidentiality concerns that eircom and other stakeholders may have.

Application of the Tilted Annuity Depreciation Methodology

Vodafone agrees with ComReg's proposal to use the tilted annuity depreciation methodology in deriving the annual depreciation charges of the network assets required for the provision of LLU because of the way that this method properly accounts for future prices and provides efficient investment incentives. However Vodafone is concerned by an apparent inconsistency between ComReg's description, in paragraph 4.37 of the consultation, of the impact of the trend of asset prices on the annual depreciation charges over time when using the tilted annuity formula, and Vodafone's understanding of the effect of this formula. Indeed the description of the effect of the tilted annuity formula in paragraph 4.37 is to Vodafone's knowledge entirely incorrect and the exact opposite of its actual effect.

Specifically it is Vodafone's understanding that if asset prices are falling then the tilted annuity formula allows for <u>higher</u> depreciation charges in the early years, and if asset prices are rising then the tilted annuity formula allows <u>lower</u> depreciation in the earlier years. Vodafone also notes that the application of specific figures to the tilted annuity formula as set out in Appendix C of the consultation document indicates that the effect of the formula is consistent with Vodafone's view and contrary to that as set out by ComReg. It may be the case that there may simply be an error in the description of the impact of use of the formula by ComReg in paragraph 4.37 and that the formula itself has been used correctly in deriving the final proposed LLU monthly rental charge. However clarification from ComReg on this issue is necessary as the possibility that the tilted annuity depreciation formula, as a significant factor in the determination of the LLU monthly charge, has been applied incorrectly, must be excluded. If the tilted annuity formula has in fact been applied incorrectly then this would clearly require that the proposed final LLU monthly rental charge be changed.

Response to Consultation Questions

Q.1. Do you agree that the period from 2000 to 2012 is a reasonable length of time to evaluate the price trend data for the copper access network assets? Please state the reasons for your response.

Vodafone agrees that the period from 2000 to 2012 is a reasonable length of time to evaluate the price trend data for the copper access network assets. However Vodafone does not agree with the detail of the proposed adjustment to the historical price trend by the ratio of forecast price inflation to historical price inflation as set out in paragraph 4.47 of the consultation document. Vodafone contends that the adjustment should reflect the <u>difference</u> between the historical price trend and the forecast price trend, not the <u>ratio</u> as currently proposed by ComReg.

Using the numbers provided in ComReg's example, the adjustment would therefore be: 2% - 4% = -2%. If historically the cost of digging trenches had risen at 10% per annum then it should be forecast to rise at a rate of 8% per annum (10%-2%) in the future. The alternative ComReg approach of using the ratio artificially 'gears-up' the impact of inflation. For example under the ComReg approach a 2% increase in the inflation rate results in a 5% increase in the cost of digging trenches. There is no methodological or economic rationale for use of such an assumption. Vodafone recommends that our suggested approach is therefore a superior method to adopt.

Vodafone agrees that the particular copper price and proposed 5% annual price trend proposed to be used by ComReg for the 'copper' part of ComReg's network are reasonable to use for the period of the proposed price control.

Q2. Do you agree that the basis used for forecasting price trends for copper and the other local loop assets (ie. poles, trenches, chambers, MDFs, street cabinets, etc) appears reasonable? Please state the reasons for your response.

Please see the response to question 1.

Q3. Do you agree that it is reasonable to consider that contractor costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

No. While labour costs have recently declined, this is a very rare occurrence in a historic context. Like the current general price deflation as measured by the most recent monthly reports for the consumer price index (CPI), the decline in labour costs is very likely to be a transitory phenomenon that will end with even a mild cyclical upturn in the economy and the return to the usual trend of a rising CPI on a year on year basis. Vodafone considers that a reasonable assumption would be for labour costs to begin to rise again in nominal terms, albeit at a modest annual rate of 2-3%, after 2010.

Q. 4. Do you believe that the volumes of working lines will increase, decrease or remain static over the proposed price control period? Please state in percentage (%) terms your views on the likely movements with detailed calculations, if necessary.

Vodafone agrees that the recent decline in the number of working lines is a short term phenomenon. Growing broadband penetration, the increasing performance of broadband services in terms of speed and other attributes, and intensifying competition in the fixed line communications sector over the price control period will stimulate demand and cause the volume of working lines to increase significantly over the next 3 years.

Q. 5. Do you agree with ComReg's preliminary view that working capital should not be included in the BU-LRAIC cost model used to determine the LLU monthly rental charge? Please state the reasons for your response.

Vodafone disagrees with ComReg's preliminary view that working capital should not be included in the BU-LRAIC cost mode used to determine the LLU monthly rental charge. It must be recognised that eircom obtains line rental revenues from OAOs two months in advance and that this is a significant benefit to eircom in terms of negative working capital (ie. customers are part-funding the access line business). This factor must therefore be reflected through including working capital as an element in the BU-LRAIC cost model used to determine the LLU monthly rental charge.

Q. 6. Do you agree that it is reasonable to consider that labour costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

No. Vodafone's reasoning in respect of the future trend in labour costs is the same as that previously set out with regard to the future trend in contractor costs as set out in the response to question 3. While labour costs have recently declined, this is a very rare occurrence in a historic context. Like the current general price deflation as measured by the most recent monthly reports for the consumer price index (CPI), the decline in labour costs is very likely to be a transitory phenomenon that will end with even a mild cyclical upturn in the economy and the return to the usual trend of a rising CPI on a year on year basis. Vodafone considers that a reasonable assumption would be for labour costs to begin to rise again in nominal terms, albeit at a modest annual rate of 2-3%, after 2010.

Q.7. Do you agree that the LFI of the current Eircom network is not an appropriate basis on which to set the operating costs of a BU-LRAIC model in determining the LLU and SLU monthly rental charge? Please state the reasons for your response.

Vodafone agrees that the LFI of the current Eircom network is not an appropriate basis on which to set the operating costs of a BU-LRAIC model in determining the LLU and SLU monthly rental charge as that LFI is based on a legacy network which is not efficient. Legacy issues around the current eircom network, such as the age of many elements of that network, would lead to much higher LFI than the model of an efficient network on which the regulated prices of LLU and SLU monthly rental must properly be based.

Q. 8. Do you agree that the LFI of an efficient BU-LRAIC model, used to determine the LLU and SLU monthly rental charge, should be based on an LFI not exceeding 8%? Please state the reasons for your response.

Vodafone agrees that a LFI not exceeding 8% is appropriate to use in an efficient BU-LRAIC model as it is in our view consistent with the likely outcome of an efficient new network.

Q. 9. Do you agree with the overall preliminary approach taken by ComReg above in relation to the basis used in determining the capital costs and operating costs used in the BU-LRAIC model for determining the monthly rental charges of LLU and SLU services in Ireland? Please state the reasons for your response.

There is insufficient information available to Vodafone to provide any firm views on the preliminary approach taken by ComReg in relation to the basis used in determining the capital costs and operating costs to be used in the BU-LRAIC model. We acknowledge that given the confidential nature of much of this information, full transparency cannot be provided by ComReg on these costs. Nonetheless the lack of information seriously limits the capacity for Vodafone and other interested parties to provide informed comment on the proposed costing approach and we would urge ComReg to consider whether additional information can be provided while still addressing legitimate confidentiality concerns. Vodafone notes for example that in paragraph 4.118 of the consultation, where the approach to the distance between telegraph poles in the modelling exercise is discussed, it is not disclosed what engineering rule on pole distance has been used to model this parameter despite the fact that we consider that this could not possibly be regarded as commercially sensitive information warranting protection on confidentiality grounds.

Without prejudice to Vodafone's views on the lack of sufficient information for respondents to make conclusive statements on the appropriateness or otherwise of ComReg's approach to capital and operating costs, provisionally the high level description of the method adopted by ComReg appears in many respects to be broadly consistent with the approach that Vodafone believes should be adopted. Vodafone agrees for example that implementing efficiency adjustments of the type that ComReg indicates it has made are correct in principle, although the lack of information on the extent of the adjustments precludes comment on whether these adjustments are adequate.

Vodafone must question why ComReg has not benchmarked ComReg's operating costs and indirect capital costs against those of U.S. LECs in the current modelling exercise as ComReg indicated was carried out by it in 2004. It is Vodafone's understanding that this benchmarking approach has been used by regulators in the U.K. and France in informing the setting of regulated prices in those jurisdictions and, although it is not sufficient to employ this approach on its own, it could usefully highlight whether eircom's costs are significantly above efficient operator levels.

Q. 10. Do you agree that the fault clearance charge should remain a separate charge from the LLU monthly rental charge? Please state the reasons for your response.

Vodafone agrees that the fault clearance charge should remain a separate charge from the LLU monthly rental charge. It would be inefficient to recover the cost of clearing faults from the LLU monthly charge when the driver of these charges, the instance of faults, is separate from the factors determining the underlying efficient costs of the SMP operator providing access on the basis of LLU. Vodafone also accepts that having a separate line fault charge creates proper incentives for OAOs to take actions to minimise the number of faults that are reported.

Q. 11. Do you agree that exchanges with working lines in excess of 1,600 is a reasonable cut-off for those exchanges that are unlikely to be economically viable for OAOs to unbundle in the timeframe of the proposed price control period? Please state the reasons for your response.

No. While Vodafone agrees with ComReg's proposed overall approach of making a distinction between exchanges that are more or less likely to be unbundled and using a probability weighting approach to determine the revised LLU price, the proposed threshold that exchanges with under 1,600 working lines should be regarded as unlikely to be feasible to unbundle in the control period is inappropriately low and ComReg has entirely failed to provide effective justification for this.

None of the points set out by ComReg in section 5.10 of the consultation explaining ComReg's reasoning provide a robust economic rationale for the selection of the proposed 1,600 working lines threshold for exchanges that are likely to be feasible to unbundle. In paragraph 5.10.1 of the consultation ComReg offers as support for its decision in drawing the distinction between large and small exchanges at the 1,600 lines level that it:

> *"Is in fact significantly lower than the number of lines coming from the smallest exchange currently unbundled in Ireland."*

Further, in paragraph 5.10.3 ComReg states:

> *"Would mean that in the context of current levels of unbundling, only 35% of those exchanges considered likely to be feasible for unbundling in the period (i.e. those exchanges with more than 1,600 lines) currently contain any unbundled DSLAM;"*

These statements are truisms rather than evidence in support of the particular threshold proposed, and Vodafone does not see how these points have any relevance to establishing that the threshold chosen by ComReg is a reasonable reflection of the economic cut-off point for alternative operators between those exchanges that are likely to be feasible for them to unbundle, and those that are unlikely to be unbundled.

In paragraph 5.10.4 of the consultation document, ComReg offers that the proposed threshold:

> *"Appears to be conservative based on the interviews that ComReg has held with OAOs that are currently active in the market; as well as those that are considering entering the market."*

While it is appropriate that ComReg has considered the inputs provided by OAOs on this issue in the course of previous interviews, it is unclear how the threshold selected by ComReg actually relates to the information provided. ComReg states that the 1,600 working lines cut-off point appears to be 'conservative' based on information on this issue provided by OAOs. It has not been specified by ComReg how this principle has been applied, but Vodafone considers that it is reasonable to assume that either the lowest estimates of exchange sizes (in terms of working lines) mentioned by OAOs, or a figure below even the lowest estimates provided by OAOs were used in coming to the 1,600 working lines threshold.

Vodafone contends that it is entirely inappropriate for ComReg to employ a 'conservative' approach in the manner that it appears to have done, both in relation to the specific issue of determining the cut-off point between large and small exchanges and more generally in other aspects of the BU-LRAIC cost modelling exercise that has been undertaken. With regard to the proposed working lines threshold, the particular manner of implementation of this principle appears to have had the effect of introducing a systematic downward bias in the assessment of the appropriate cut-off point for exchanges that can be feasibly unbundled, and consequently introducing a systematic upward bias into the determination of the LLU monthly rental charge. The introduction of this upward bias into the determination of the revised LLU monthly rental charge has no defensible methodological, economic efficiency, or consumer welfare justification, and ComReg has not attempted to provide one. Indeed the use of this approach is entirely counterproductive to the achievement of ComReg's statutory regulatory objectives, in particular the promotion of competition and the promotion of the interests of end users, as it unjustifiably reduces the scope for OAOs to compete robustly with eircom in the retail market on the basis of use of LLU inputs and therefore precludes consumers from realising the full potential benefits of optimally priced LLU wholesale inputs for OAOs in terms of lower prices and differentiated communications service offerings. Vodafone therefore urges ComReg to adopt an alternative approach to determining the optimal cut-off point for exchanges that can likely be feasibly unbundled that is based on evidence of costs that OAOs actually face, and which does not unjustifiably bias upward the LLU monthly rental charge as the current proposed exchange size threshold appears to do.

In addition, and from a practical perspective, Vodafone considers that the information on exchange sizes likely to be feasible to unbundle that OAOs have provided ComReg with, and in particular the lowest estimates provided, can not be regarded as determinative of the issue of the appropriate cut-off point (in terms of working lines) to be used in the probability weighting approach. This is because these estimates were likely based on expectations of a reduction in the LLU monthly rental charge as a result of the current review, the rental charge being a key cost input in OAOs assessment of the extent to which unbundling would be viable, considerably greater than that now being proposed by ComReg.

Vodafone notes that the remaining reason offered by ComReg, in paragraph 5.10.2, in support of the preliminary view that exchanges with less than 1,600 lines are unlikely to be feasible for unbundling is that this threshold is consistent with the smallest exchanges that are unbundled in France and lower than that in the UK. Vodafone does not understand why ComReg considers France to be the most appropriate benchmark in terms of the determining the cut-off point at which exchanges are unlikely to be viable to unbundle, and no detailed reasoning has been set out to justify this view in the current consultation. In particular, ComReg's view that France is a more appropriate benchmark than the U.K. in this respect requires a detailed explanation as it is inconsistent with ComReg's view as set out in ComReg's consultation document on the Review Regulatory Asset Lives of Eircom (ComReg document 09/11) that the regulatory asset lives used by BT Group were of particular relevance in determining the appropriate asset lives for Eircom given the similarity of many parts of the U.K. to Ireland in terms of topography and other factors.[1] It is Vodafone's view that, where a benchmarking approach is applied, the U.K. is the most suitable peer country in informing the decision on the optimal cut-off point between large and small exchanges.

As ComReg has indicated in the consultation, the evidence from the U.K. is that exchanges with less than 2,500 lines are not normally unbundled by OAOs and this is also consistent with the fact that the smallest exchange currently unbundled in Ireland has in excess of 2,700 lines. Vodafone would emphasise in the first instance that the threshold for determining exchanges that are likely to be unbundled during the review period should be based on evidence of costs that OAOs actually face in Ireland, but information from the U.K., the most relevant comparator country, indicates that the optimal threshold should approximate 2,500 working lines rather than the 1,600 lines cut-off point currently proposed by ComReg. Vodafone recommends that ComReg should therefore change the parameters of its LLU costing methodology accordingly.

Q.12. Do you agree that it is unlikely that an OAO would unbundle a line unless it was able to provide broadband services over that line; and do you agree that 5 km represents the maximum line length that may be used for these services? Please state the reasons for your response.

Vodafone considers that OAOs would not unbundle lines if they were not able to provide broadband services over that line. On the basis of the available information, and the fact that 5 km is the maximum line length for broadband services used by eircom itself, Vodafone agrees that a 5km maximum is reasonable to use in determining the regulated LLU monthly rental charge.

[1] *ComReg doc 09/11 – 'Consultation & Draft Decision: Review of the Regulatory Asset Lives of Eircom Ltd.', paragraph 2.8*

Q. 13. Do you agree that ComReg's proposal is conservative in that it includes an element of the costs associated with lines in excess of 5 km?

Yes, we agree that ComReg has taken a conservative approach but Vodafone entirely disagrees with ComReg's application of its conception of a 'conservative' approach to the costs of long lines in the determination of the LLU monthly rental charge. As set out in the response to question 11, Vodafone considers that ComReg's current general 'conservative' approach involves employing a form of costing methodology that introduces a systematic and substantial upward bias into the determination of the LLU monthly rental charge. This approach cannot be justified on methodological, economic efficiency, or consumer welfare grounds.

As it is neither economically nor technically viable for OAOs to unbundle long lines (> 5 km) over which they are not able to provide broadband services, there is no basis whatever for any element of the incremental costs of long lines to be included in the calculation of the LLU monthly charge. Indeed the preliminary view of ComReg in its initial consultation on proposals for local loop unbundling pricing methodologies (ComReg document 08/56) was consistent with Vodafone's position. In paragraph 5.32 of that consultation document, ComReg stated:

> *"ComReg also considers that copper lines that are too long are unlikely to be unbundled by OAOs. This is because DSL capabilities reduce the longer the length of the copper line. After a certain distance from the exchange the provision of broadband, via DSL, is not possible.* ***Accordingly, ComReg is also considering combining Option C with Option B by excluding long lines from areas that are otherwise potentially viable****."* [Vodafone emphasis in bold]

It is clear that at the time of ComReg's initial consultation on LLU pricing methodologies, it was envisaged that long lines would be totally excluded from the calculation of the costs underlying the LLU monthly rental charge. Vodafone agreed with this proposal in our submission to that consultation for the reasons set out by ComReg and we consider that nothing has changed in the interim to alter the validity of this position. ComReg's proposal in the present consultation that some element of the incremental costs of long lines must now be included in the calculation of the LLU monthly rental charge therefore represents a fundamental reversal of its original stance. ComReg's change of position on this issue therefore at a minimum requires extensive justification, but there is not even an acknowledgment in the consultation document that ComReg's proposed approach to the treatment of the cost of long lines has changed since consultation document 08/56 was published. Vodafone considers that the absence of any justification for ComReg's proposed change of approach other than the invalid one that it would in ComReg's view 'enhance the conservative nature of the calculation' means that the costs of long lines must therefore be excluded totally from the determination of the LLU monthly rental charge.

Q. 14. Do you agree with ComReg's proposed weightings, as set out above, used in relation to the cost associated with long lines and small exchanges? Please state the reasons for your response.

Vodafone agrees only in part with the proposed weightings to be used by ComReg in relation to the cost associated with long lines and small exchanges.

Vodafone considers that it is appropriate and reasonable that 95% of the cost of lines in large exchanges and 5% of the cost of lines in small exchanges are included in the calculation of the regulated LLU monthly rental charge. The 95:5 ratio is a good approximation of the likely distribution of unbundled lines between large and small exchanges respectively and has the benefit that the costs of all exchanges will be incorporated to some extent in the determination of the final regulated LLU monthly rental charge.

For the reasons set out in response to question 11 however, Vodafone considers that the proposed cut-off point of 1,600 working lines proposed by ComReg to distinguish between large and small exchanges is inappropriately low and has not been effectively justified. It is our view that the determination of the optimal cut off point between large and small exchanges for the purpose of determining the final weighted average LLU monthly rental charge should be based primarily on evidence of costs that OAOs actually face in Ireland in unbundling exchanges. Vodafone contends that the appropriate threshold approximates 2,500 working lines, consistent with that observed in the U.K. and also in line with the fact that the smallest exchange unbundled in Ireland to date has in excess of 2,700 working lines. Use of the alternative threshold recommended by Vodafone will significantly reduce the number of exchanges included in the 'large exchange' category for the purposes of calculating the LLU monthly rental charge compared with ComReg's current methodology.

For the reasons set out in response to question 13, Vodafone also strongly disagrees with ComReg's current proposal to attach a positive (5%) weight to the costs of long lines in excess of 5 km in the calculation of the regulated LLU monthly rental charge. As it is neither economically nor technically viable for OAOs to unbundle long lines over which they are not able to provide broadband services, there is no basis whatever for any element of the incremental costs of long lines to be included in the determination of the LLU monthly charge. ComReg must therefore revisit its current methodology and assign a zero weighting to the costs of long lines in assessing the LLU monthly rental charge (entirely excluding any costs associated with long lines from the calculation).

Q. 15. Do you agree that the charge at option 4 is the most appropriate charge for setting the LLU monthly rental charge going forward? Please state reasons for your response.

Vodafone does not agree that the charge of €12.18 at option 4 is the most appropriate charge for setting the LLU monthly rental charge going forward. This is because the charge is based on incorrect assumptions made by ComReg, described by Vodafone in the response to previous consultation questions, relating for example to the forecast evolution of key costs relevant to the provision of LLU. In addition the proposed €12.18 charge is inappropriate for the reasons set out in the response to question 14, particularly the use of an excessively low cut-off point for the purposes of defining large versus small exchanges and the inclusion of an element of the incremental cost of long lines in the calculation of the LLU monthly rental charge.

All the other options for charges proposed by ComReg (options 1-3) as set out in the table following paragraph 5.29 in the consultation document are however even more seriously flawed than Option 4 as the methodology underlying them is even less reflective of the underlying efficient costs of the provision of LLU than the approach currently proposed by ComReg. Vodafone considers that the first-best option for the setting of the LLU has not been explicitly set out by ComReg in the consultation. This optimal approach would require the use of revised assumptions and a different weighting approach to that used by ComReg in a number of key respects, on the lines set out by Vodafone in response to previous consultation questions. Vodafone urges ComReg to revisit its approach and adopt our proposals in order to determine a regulated LLU monthly rental charge that most accurately reflects the underlying efficient costs of the provision of LLU to OAOs. This will facilitate enhanced and sustainable competition in the market between eircom and OAOs on the basis of use of LLU inputs on reasonable terms. This can only be to the benefit of end users of communications services going forward.

Q. 16. Do you agree that the charge at option 2 results in the most appropriate charge for setting the SLU monthly rental charge going forward? Please state reasons for your response.

No. Vodafone notes that the SLU charges reflect the costing parameters set out in Section 4 of the consultation document and we consider that different parameters to those proposed by ComReg should be implemented in some respects. These changes will lead to a different proposed charge than that set out by ComReg as option 2 in the table following paragraph 5.33 in the consultation document. Vodafone does however agree with ComReg's high level conclusion that sub loop unbundling is highly unlikely to happen outside the major urban areas identified by ComReg within the time period of this review. The finding of Analysys Consulting that only street cabinets with a minimum of 300 lines would be economically viable for the purposes of sub loop unbundling is also reasonable.

Q. 17. Do you believe that given the current economic circumstances that a proposed price control period of three years with a review in year 2 is the most prudent option? Please state the reasons for your response.

Vodafone agrees that the proposed price control period of three years is the most prudent option. However we must question the rationale for a review in year 2, as this significantly reduces the intended benefit of regulatory certainty from the selection of a 3 year control period. It is vital for the business planning of OAOs that they have the greatest possible visibility of the level of the LLU and SLU access charges over the medium term and Vodafone therefore recommends that ComReg should revise its current proposal to exclude the proposed element of a review in year 2.

Vodafone agrees that ComReg must have discretion to intervene in the setting of the LLU and SLU access charges within the 3 year price control period if exceptional circumstances warrant. The examples of exceptional circumstances set out by ComReg in paragraph 5.37 of the consultation document indicate however that the current definition of 'exceptional circumstances' is too broad and would greatly limit regulatory certainty for market participants. Vodafone recommends that two criteria should be clearly established at the outset to determine changes that could be regarded as exceptional ones warranting intervention by ComReg within the price control period. The suggested criteria are:

1. The changes make a material difference to eircom's actual cash outflow
2. The changes are outside the control of eircom

Labour costs increasing above forecasts would, for example, on the basis of these criteria not meet the requirements for exceptional intervention by ComReg if eircom had made a discretionary decision to introduce the above forecast pay increases.

Q. 18. Do you believe that the draft decision is clear, precise, and intelligible from a legal, technical, and drafting perspective? Please state the reasons for your response.

Vodafone agrees that the text of the draft decision is appropriate and correct from a legal, technical, and drafting perspective.

Q. 19. Respondents are invited to comment on the draft direction from a legal, technical and drafting perspective as set out above.

Vodafone does not have specific comments on the legal, technical, and drafting aspects of the draft decision.

Q. 20. Respondents are requested to provide views (if any) which ComReg should consider in completing its Regulatory Impact Assessment.

Vodafone agrees with the high level preliminary conclusion of ComReg's Regulatory Impact Assessment (RIA) that Option 3 is the optimal approach to undertake as Options 1 and 2 would not be in compliance with maintaining the obligation of cost orientation on eircom. The 3 options considered by ComReg are in Vodafone's view the relevant ones to be assessed in the analysis and do not appear to omit any viable additional alternatives that should also be assessed. The RIA conducted by ComReg to date is in Vodafone's view sufficiently demonstrates that the general approach adopted by ComReg (Option 3) is appropriate, justified and proportionate to undertake. The conclusions of the RIA would however be further strengthened if ComReg, in completing the RIA, were to quantify where feasible the benefits and costs of its proposed option relative to the alternatives set out.

3 Smart Telecom

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Director of regulatory affairs
Smart Telecom Holdings Ltd
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Ms. Claire Kelly
Commission for Communications regulation
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June 2009

ComReg 09/39 – Smart Telecom response – Public version

Dear Claire,

Smart Telecom welcomes Comreg's above mentioned consultation and draft decision. **It is now vitally important to immediately move to a final decision.**

Main Points :-

- **Smart Telecom would like to acknowledge the large degree of work that has obviously gone into the draft decision and consultation.**
- **Overall, Smart Telecom welcomes the proposed price reduction but is disappointed at the extent of the reduction and the proposals on repair costs. A line price closer to €10.00 is vital to attract investment and this can be easily achieved within the new control.**
- **While very welcomed, the proposed price still leaves Ireland the 4th most expensive in Europe and is very unlikely to attract new players to the Irish Market relative to competing nations. Smart Telecom will outline how, using the same methodology, a more attractive price can be achieved.**
- **Since the publication of the proposal eircom has finalized details of a significant costs reduction plan with more to follow also of note are deflation figures for Ireland have been confirmed at approx 3.5% for 2009 YTD.**
- **We believe the long : short line weighting ratio is disproportionate and needs to be adjusted.**
- **We believe a more aggressive and practical approach is required to drive investment in LLU and attract new investment.**

Kindest Regards,
John Quinn

Answers to consultation questions

Q. 1. Do you agree that the period from 2000 to 2012 is a reasonable length of time to evaluate the price trend data for the copper access network assets? Please state the reasons for your response

Yes. Smart Telecom, in general, believe that any period in excess of ten years is going to give an overall representative view on pricing data however we are currently in an economic environment not seen since the 1930's. The years 2008-2012 will be a critical period for Ireland and will not follow the norms of 2000-2007.

While Smart Telecom agree that CPI trends do not always follow pricing trends, we do note that eircom have applied CPI increases to LLU and retail prices in recent years.

Smart Telecom question the weighting used in ComReg 09/39 section 4.48 and we do not believe that the weighting goes far enough to reflect current realities. The ESRI has indicated unemployment rates of up to 16.8%[1] by the end of 2010 causing a dramatic lowering of labour rates and associated benefits. Indeed many are predicting a period of up to ten years or more to see employment levels return to 2007 levels and longer for standards and rates of pay.

Smart Telecom also notes that CPI for 2009 is likely to be negative to the tune of 3.5% given recent announcements on CPI. "services" for the period were running at negative 3.2%.

In this regard, and to reflect reality, we believe that the 2008-2012 period should have a factor weighting of an additional 50%. As BU-LRAIC models are forward looking (not regressive) this also matches the time frame to the model.

Fig 1 – CPI& HICP –CSO

Consumer Price Index
April 2009

CPI and HICP

	CPI		HICP	
	% monthly change	% annual change	% monthly change	% annual change
Dec 2008	- 1.2	+ 1.1	- 0.7	+ 1.3
Jan 2009	- 1.7	- 0.1	- 0.9	+ 1.1
Feb 2009	+ 0.4	- 1.7	+ 0.2	+ 0.1
Mar 2009	-	- 2.6	+ 0.1	- 0.7
Apr 2009	- 0.9	- 3.5	+ 0.1	- 0.7

[1] http://www.esri.ie/publications/latest_publications/view/index.xml?id=2738

Q. 2. Do you agree that the basis used for forecasting price trends for copper and the other local loop assets (i.e. poles, trenches, chambers, MDFs, street cabinets, etc) appears reasonable? Please state the reasons for your response.

Smart Telecom agrees with ComReg's methodology but does not believe that the assumptions used in copper pricing are correct.

As industrial output falls, commodity pricing reacts accordingly. Metals such as copper and Zinc are sensitive to economic activity and as can be seen in copper mines (Rio Tinto et al) in copper producing countries, demand is falling while there is a growing over supply. In the commodity market, this causes prices to drop.

The gains shown in recent months are short lived and fueled mainly by restocking in China, which is a finite exercise. In recent weeks, fluctuations are now again being experienced and reflected in the LME.

Analysts say copper faced weakness in coming months as supportive buying from China tails off and ahead of a seasonally quiet market period.

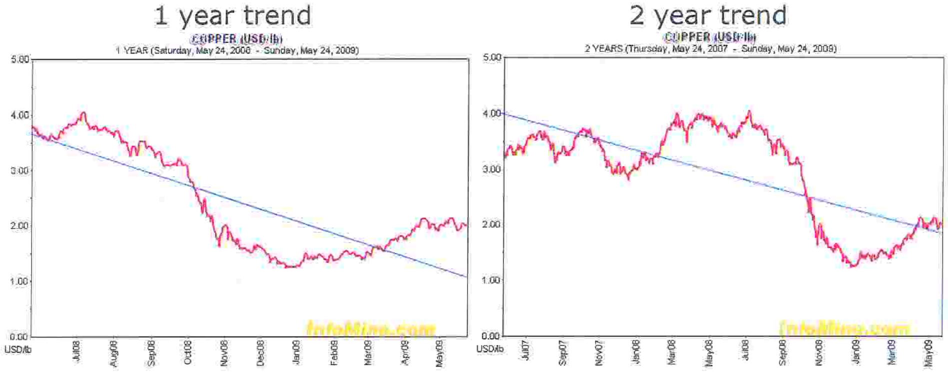
"The buying spree that China went on in the first half of the year is going to be very difficult to sustain because it was largely fuelled by restocking, which is a finite process," said Gayle Berry, metals analyst at Barclays Capital in London *(May 2009)*

"As a result we're going to see imports fall back over the next few months which, together with a seasonally weaker period for northern hemisphere demand, and continued concerns on the macro front, means it's going to be a tough couple of months for metal prices."[2]

Over the past 3 years copper prices dropped dramatically from an output peak in 2006 & 2007 to levels seen in 2005. The 3 year pricing trend is declining for each year in question.

Fig 2 – Copper pricing trends – 1, 2 & 3 year view- infomine[3]

1 year trend 2 year trend



3 year trend

[2] http://www.businessworld.ie/livenews.htm?a=2421879
[3] http://www.infomine.com/Investment/HistoricalCharts/ShowCharts.asp?c=copper

On May 20, 2009, the International Copper Study Group's (ICSG[4]) preliminary data showed that world copper production outpaced refined usage by 86,000 tons in the first two months of 2009, compared to a production deficit of 61,000 tons the previous year.

So far in 2009, world refined production is up slightly while refined usage is down 4%. In 2008, world refined production exceeded consumption by 234,000 tons. On April 21, 2009, **the ICSG predicted that copper will show a world production surplus of 345,000 tons in 2009 and 418,000 tons in 2010**.

This over production, coupled with existing drops in prices will keep copper prices steady or declining for several years to come with an upward sustainable recovery only expected[5] approaching 2013, i.e. the period of the next review but not this one.

Equally we believe that the inflation seen in the costs of civil works for trenches, chambers and digs has returned to that seen in prior to the construction boom years and is now downward. This is being reflected in current prices being seen in RFIs being issued for civil works which in some case are at 2005 levels.

We would also bring ComReg's attention to recent reductions in energy pricing and the likelihood of the CER further reducing energy prices later in 2009 and 2010.[6]

The reductions in civil "hard" works such a duct installation, chamber digs and contractor rates are well documented with reductions of up to 40% being seen over peak 2007 rates.

Overall Smart Telecom believes ComReg has done an excellent job in looking at the options, assessing the risks of each and estimating outcomes. However the reality is that the next few years in Ireland and going to be a time of raised unemployment, lower costs, lower prices and lower input costs and this can not be ignored.

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4 http://www.icsg.org/index.php?option=com_docman&task=cat_view&gid=13&Itemid=61
5 http://www.theaustralian.news.com.au/business/story/0,28124,25540822-36418,00.html
6 http://www.cer.ie/en/information-centre-newsletters.aspx

Q. 3. Do you agree that it is reasonable to consider that contractor costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period

Yes, this is perfectly reasonable and expected.

We would estimate that labour rates for semi-skilled work to drop between 20-40% depending on the type of work being undertaken.

As widely reported many employers have sought and secured wage reductions of between 10-20%. However, as many lay offs have occurred within the construction industry competition for lower end jobs is high with many now willing to work at vastly reduced rates. While this is both an ethical question as well and an economic one it does reflect the likely reduction in costs.

Also supporting this is the Hudson Salary guide for 2009 in which it is stated that telecoms engineers will be likely to see a salary of between €32,000 to €55,000, (lower & upper scale levels). (full report included)

Q. 4. Do you believe that the volumes of working lines will increase, decrease or remain static over the proposed price control period? Please state in percentage (%) terms your views on the likely movements with detailed calculations, if necessary

We agree that the number of working lines will remain static or marginally decrease for a number of reasons:-

- The slow down in new construction development
- The move to "mobile only households"
- The move to save money in recession
- The Growth of Cable

It is difficult to predict how this will play out in % terms as Ireland has a large % take up of landlines to date compared, for example, to the USA where mobile only households are growing rapidly. Factors such as mobile MTR rates etc will also influence movements.

The deployment and upgrading of 2-way cable systems and DOCSIS 3.0 will also have an impact on the take up of phone lines versus packet voice cable based services. This can be seen already in eircom's result to Quarter ended March 2009 with PSTN lines dropping.[7]

On a more general note - It should be noted that there now appears to be a trend beginning toward the reduction of PSTN lines. Smart would view LLU as a key enabler to drive the uptake of PSTN services in general. It should also be noted that there are several hundred thousand PSTN lines lying idle in Ireland, mainly in new housing developments with younger families opting not to invest in a PSTN service at all. LLU can also address this market and indeed there is no retail threat to *eircom* in this regard, in fact a first time connect to LLU gives *eircom* retail the opportunity to "win" the customer from the LLU operator.

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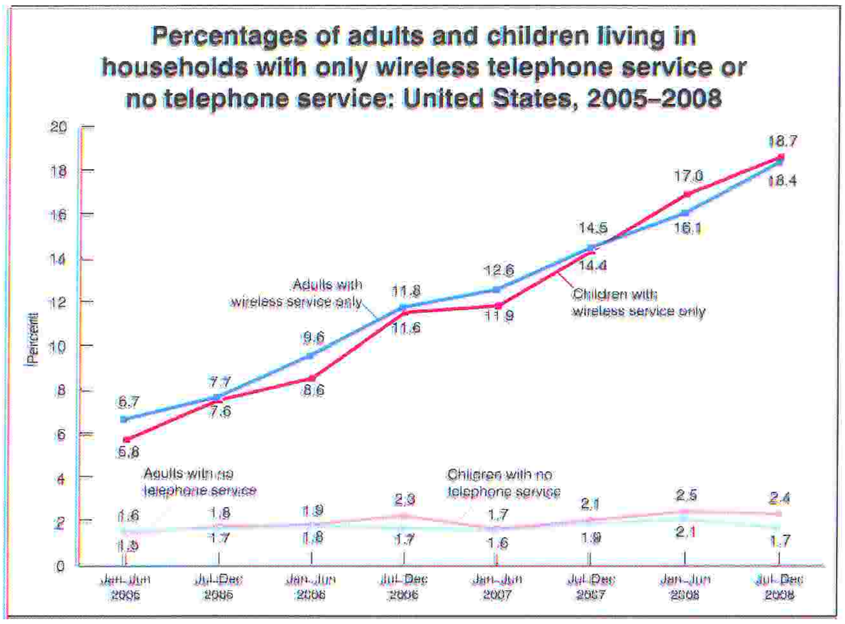
[7] http://home.eircom.net/about/press/2009/May/15753752?view=Standard&main=yes

A recent report from the USA shows an interesting and worrying trend towards "mobile only" usage

Fig 3 – USA Mobile only households – NCHS USA



We would urge *eircom* to accept that PSTN services are under threat and that global trends relating to PSTN reductions could easily come to pass here, in particular in recessionary times.

It is estimated that up to 20% of American households are now "Wireless only"[8]

AT&T, for example, has noted that landline customers were decreasing significantly as early as last year; in its most recent quarter, the company got less than 30 percent of its revenue from wired voice customers, and more than 40 percent from wireless customers. Similarly, Verizon saw landline subscribers decrease by 4 million, while wireless subscribers increased by 20 million.

A large decrease in PSTN services will hamper investment decisions for NGN and also have large scale employment and social and economic benefit implications. ComReg MUST act in a brave and forward thinking manner in order to protect consumers and PSTN services for all operators, including *eircom*.

Finally the proposed revised price for LLU, while welcome, does not go far enough to attract new market entrants which would drive PSTN lines, it has to be closer to €10.00.

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[8] http://blogs.zdnet.com/gadgetreviews/?p=4124

4 BT Communications Ireland Ltd.

BT Communications Ireland Ltd response to the ComReg Consultation:

Further Consultation on Local Loop Unbundling ('LLU') and Sub Loop Unbundling ('SLU') Monthly Rental Charges

Issue 1 12/06/2009

Introduction

BT welcomes the opportunity to comment on this consultation dealing with the key broadband service and competition stimulant known as Local Loop Unbundling (LLU). Achieving the correct cost orientated price for LLU has proven in other countries (most recently Greece) to stimulate competitor investment, stimulating differentiation in broadband services, stimulating the incumbent to upgrade its services and stimulating greater retail competition. LLU could even stimulate greater use of eircom's access network as more players would be become interested in DSL based solutions and offer a wider and more competitive range of products.

Regrettably LLU in Ireland is a story of lost opportunity; prices for LLU in Ireland are the highest in Europe, see Annex A.

It is public domain knowledge that the progress of LLU in Ireland has been painfully slow and this is set out on the ComReg web site through numerous directions other action against eircom.

Whilst we would still like to believe that LLU has a real part to play in Next Generation Broadband in Ireland, it will only play that part when prices for all LLU components are slashed. It would be a brave operator to predict when that might be and thus delay in regulatory progress always results in delayed investment by alternative operators.

Price Reductions

BT considers that the proposed price reductions (16.43 Euros per month to 12.12 Euros per month rental) is of little value as its only a part charge and does not reflect the 'net' real line rental which is closer to 13.26 Euro per month once maintenance is included. BT is of the view that the LLU line rental price including maintenance should be closer to 9.95 Euros per month.

- The 12.12 Euro line rental needs to be qualified that it does not include maintenance hence is in reality only a part charge. Given the poor state of the eircom access network BT observes that it would have to pay an additional repair charge per year and this will provide the 'net' rental per customer. If as detailed in clause 4.130 of the ComReg consultation the Line Fault Index is 12.5% this would mean that each line has a 12.5% probability of going faulty each year. This would have a cost implication of 12.5% multiplied by 117 Euro or 109.7 Euro (the eircom price per repair) per year per line. I.e. an additional charge per month on each line of either 1.22Euro or 1.14Euro depending on the fault order type used.   Hence the headline price is more realistically 12.12+1.14 = 13.26 Euro per month.

- BT is also finding it difficult to reconcile some of the ComReg modelling logic. BT understands from the consultation that the model is designed to apply for areas where LLU is likely to be deployed, hence ComReg suggest the Line Fault index should be reduced and thus repair costs reduced, however, maintenance has been kept outside of the rental price so it's not clear how the benefit applies. The application by eircom of a repair per incident price negates any linkage to savings for the service being in more urban areas with underground cabling.

- BT considers that LLU rental should be normalised and the maintenance charge should be included in the rental charges particularly as the line fault index is so high and LLU operators are required to pay for repair on a per incident basis, unlike other eircom services. Per incident charges provide no incentive for eircom to improve their service quality unlike for other eircom services where eircom takes the risk by factoring repair costs into the fixed rental charge. The eircom ARO price list acknowledges that operators can provide the line test information, and given this acknowledgement the line rental should include maintenance where the line information is supplied. This will align LLU with other eircom products such as Wholesale Line Rental. Hence where test results are supplied there should be no separate charge but a different monthly rental.

- Other countries appear able to hit significantly lower prices of around 8.29 Euro per month for LLU line rental with repair charges included. At 13.26 Euro per month Ireland is still out of kilter with Europe.

- BT is of the view that the proposed price minus the maintenance charge is of little value and will not address the competition issue in this market. BT considers that the cost saving announced by eircom should be factored into the cost model and assuming these will be in the order of 25% given headcount reductions, closing costly buildings etc, the reasonable and fair LLU monthly rental price would be in the order of 25% multiplied by 13.26 Euro which would equate to an LLU line rental price of 9.95 Euros per month including repair.

- The only real driver to reduce prices will come when eircom are mandated to purchase the same services at the same prices and performance that they supply to the other operators. Only then will the eircom have the appropriate cost and performance signals to improve their wholesale products.

Discrimination

BT considers that the direction needs to be re-drafted to include all the operators in the market, and specifically it should be modified to include the largest player in the market, i.e. eircom Retail as a downstream provider. Without such a modification their will be no transparency of what eircom are offering themselves; there will no incentives for eircom to improve wholesale pricing and services to the OAOs; and there remains a significant potential for eircom to discriminate against OAOs.

Inefficient Services
Whilst eircom continue to support dual systems for its own downstream provider and separately for the OAOs they are making the conscience decision to be inefficient. Regulation is aimed at encouraging efficient operators and for this reason ComReg should only allow eircom to recover such costs it would reasonably require to run single provision and assurance platforms that would offer equivalence of input to all downstream providers including its own downstream provider.

Cost Model
BT is disappointed that it was not afforded the same opportunity to have studied the costing model as was provided to eircom. BT has a considerable amount of expertise in LLU within its organisation and could have offered constructive comments based on experience of providing over 5 million LLU lines in other jurisdictions including the UK and Italy. BT is of the view going forward that any such future models should either be provided to no operator or to all interested parties.

Review Period
BT agrees with ComReg for a three year period for the new price control and strongly recommends that price reviews are not allowed to extend to some five years as has happened previously.

Detailed Response

Q. 1. Do you agree that the period from 2000 to 2012 is a reasonable length of time to evaluate the price trend data for the copper access network assets? Please state the reasons for your response. .

BT Response 1
BT agrees that the period from 2000 to 2012 is a reasonable length of time to evaluate the price trend data for copper access network assets in Ireland. BT agrees that by correlating the price trends over some 21 analysts will smooth the trend and provide greater confidence of correctness. BT agrees with ComRegs approach.

Q. 2. Do you agree that the basis used for forecasting price trends for copper and the other local loop assets (i.e. poles, trenches, chambers, MDFs, street cabinets, etc) appears reasonable? Please state the reasons for your response.

BT Response 2

BT agrees that the process proposed by ComReg is reasonable as taking the forecast over a longer period smoothes short term variations and brings both stability and certainty.

Q. 3. Do you agree that it is reasonable to consider that contractor costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

BT Response 3

- Average payment terms

BT would like to address clause 4.50 in its response to this question. BT notes the discussion in clauses 4.51 through to 4.62 has an extra complexity. Whilst BT would agree with ComReg for a situation where a significant new network infrastructure is being deployed, it does not agree that the rule is correct for the cases where a small network is being deployed or for the situation where an existing network is being used. BT considers that it is likely the lead time to revenue can be much shorter, and indeed instantaneous where existing network is being used, such as for LLU.

It should also be noted that for the case of LLU any infrastructure development is on the side of the entrant and not the incumbent.

BT agrees with ComReg that the incumbent would not need to wait for a whole national deployment before earning revenue as deployment would be made live on a roll-out basis. The eircom bitstream platform is a good example of this which is still being rolled out many years after the initial service was launched and revenue received.

Therefore BT agrees that ComReg is correct to use six months for a larger infrastructure build but considers the lead to revenue is instantaneous for the use of existing networks for LLU.

- Contractor Cost reductions
  BT agrees with ComReg that it is reasonable to consider that contractor rates will reduce over the proposed three year price control period as this is the market trend based on a number of factors such as the oversupply of labour. The downturn of construction in Ireland, followed by that of the banking system is now having a direct impact on virtually all aspects of the employment market in Ireland. The following extract from the Economic Research and Social Research Institute (ERSI) highlights the scale of the employment problems in Ireland. This level of unemployment will have a major lowering impact on contractor costs over the period of this price review due to oversupply in the labour force.

  Extract from the Economic Research and Social Research Institute (ERSI) latest press releases. (Italics added)

  30 April 2009

  ESRI Policy Conference, 2009: The Labour Market in Recession

  Following a decade of high employment growth and very low rates of unemployment, the Irish labour market is now in crisis. Employment is contracting at a very fast rate: current ESRI estimates are there will be on average 190,000 fewer people in employment in 2009 compared with 2008, and that employment will fall by a further 100,000 over the following year. Correspondingly, unemployment rates are rising at an alarming pace, with the result that the unemployment rate this year is expected to average 13 percent, and in 2010 to rise to over 16 percent. These are challenging figures for policy makers and for society at large.

  End of extract

  In addition to the above, the contractor is more exposed than many in the current environment as by their nature they tend to be on short term contracts for specific tasks, hence their rates can be rapidly reduced through reducing re-hire prices and there are no union agreements or other complexities to address.

  Additionally, as companies reduce employee headcount, it is normally easier and less contentious to let contractors go first before making permanent employees redundant. Hence contractors of all types will face lower employment rates for a considerable length of time.

Some commentators have suggested Ireland is over priced by 25% and its noted in question 6 that eircom's itself is aiming to shed somewhere between 19 and 26.5% of staff, therefore it is proposed that the reduction in contractor rates could be reduced in the order of 25% if not more.

Q. 4. Do you believe that the volumes of working lines will increase, decrease or remain static over the proposed price control period? Please state in percentage (%) terms your views on the likely movements with detailed calculations, if necessary.

BT Response 4
BT considers that the number of eircom working lines will largely be static over the control period as customers will demand higher speeds and greater high speed reliability than offered by the current generation of mobile solutions. BT notes that three of the four mobile companies operating in Ireland have now entered the fixed broadband market or are owned by a fixed broadband company operating in Ireland. It is also unlikely that the digital dividend frequencies will not be available to the mobile sector before 2013 given that the deployment of the Digital Terrestrial Television (DTT) has not yet started in Ireland and so the expected dividend frequencies are still in use for traditional analogue television. It is difficult to predict the growth of the cable industry as this will be largely dependent on future cable investment and this could be disrupted by the current recession. Additionally the introduction of the NGN and the potential for technologies such as Ethernet First Mile (EFM) may use significant groupings of lines to offer higher symmetrical speeds to business users.

BT is of the view that if the ComReg pricing decisions for LLU were to more closely reflect the cost of the LLU assets (something that has now been achieved in a number of EU countries) then LLU could actually stimulate growth in the overall number of active eircom lines due to greater innovation and the potential to bring new entertainment and TV players into the fixed market. BTs view is that eircom's very high access pricing (the highest in Europe) is foreclosing the access market and stifling investment that would make better use the eircom network.

Q. 5. Do you agree with ComReg's preliminary view that working capital should not be included in the BU-LRAIC cost model used to determine the LLU monthly rental charge? Please state the reasons for your response.

BT Response 5

BT agrees with ComReg that working capital should not be included in the BU-LRAIC cost model as such is transient and would not truly reflect the assets deployed to offer the service.

Q. 6. Do you agree that it is reasonable to consider that labour costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

BT Response 6

eircom headcount reduction.
eircom state in their end of quarter financial presentation at March 2009 that they have reduced their headcount by 661 staff for their existing 2009/2010 target. In addition eircom have also announced a significant further cost cutting programme with some 1200 employees leaving the company in two years. This level of employee reductions will impact eircoms costs. According to eircom their headcount count at the end of March 09 was 6,367 and leaving aside the 661 employees that have already left eircom in the current programme, a further reduction of 1200 will be a decrease in headcount of 19% from today's figures. It's not known whether eircom employed new people during the past scheme but it is likely that more people left eircom than joined, hence the overall staff reduction of the two scheme probably lies somewhere between 19% and 26.5% (i.e. the reduction if the previous scheme is included).

The climate in Ireland is also driving for costs to be reduced over the coming years (See question 3). BT does expect labour costs to reduce over the next three years and would expect the labour charges to reduce by 25% or greater given the staff reduction discussed above and other cost savings from the reduction in allowances and other benefits. eircom should also being experiencing considerable savings from the migration of employees from numerous prime sites in Dublin to one main site at Heuston in Dublin etc. These saving should be factored in wholesale costs going forward.

Q. 7. Do you agree that the LFI of the current Eircom network is not an appropriate basis on which to set the operating costs of a BU-LRAIC model in determining the LLU and SLU monthly rental charge? Please state the reasons for your response.

BT Response 7

BT is of the view that it should not pay for eircom's underinvestment in their access network and the exceptionally high level of faults (Line Fault Index(LFI)) that its network experiences. BT believes that the problems are due to general underinvestment and a lack of preventative maintenance by eircom in their access network.

BT therefore agrees that the Line Fault Index of the current eircom network is not an appropriate basis on which to set the operating costs of a BU-LRAIC model to set the LLU and SLU monthly charges. A principle of regulation is to encourage efficient activity and to use the current LFI is rewarding inefficient operation which could have been avoided through investment and preventative maintenance.

However BT is finding it difficult to reconcile some of the ComReg modelling logic. BT understands from the consultation that the model is designed to apply for areas where LLU is likely to be deployed, hence ComReg suggest the Line Fault index should be reduced and thus repair costs reduced, however, maintenance has been kept outside of the rental price so it's not clear how the benefit applies. The application by eircom of a repair per incident price negates any linkage to savings for the service being in more urban areas with underground cabling. Per incident charging also negates any incentive for eircom to improve its efficiency. BT is of the view that the maintenance charge should be included in the rental.

Q. 8. Do you agree that the LFI of an efficient BU-LRAIC model, used to determine the LLU and SLU monthly rental charge, should be based on an LFI not exceeding 8%? Please state the reasons for your response.

BT Response 8

BT notes that ComReg distinguish between old and new networks and whilst BT understands the difference, BT is of the view that with good management of the network, including the use of preventative maintenance it should be possible to offer a significantly better LFI than currently available from eircom. BT supports the proposed LFI that is not to exceed 8% for the next year period but believes that eircom should be under an incentive to improve this further. Whilst maintenance is kept outside of the rental, the LFI has no impact on the Line Rental Price.

Q. 9. Do you agree with the overall preliminary approach taken by ComReg above in relation to the basis used in determining the capital costs and operating costs used in the BU-LRAIC model for determining the monthly rental charges of LLU and SLU services in Ireland? Please state the reasons for your response.

BT Response 9

Other than repair being outside of the model, BT agrees with the overall preliminary approach taken by Comreg in relation to the basis used in determining the capital costs and operating costs used in the BU-LRAIC model for determining the monthly LLU rental charges and this is based on best in practice regulatory treatments and is a logical approach to this type of service modelling. ComReg’s use of consultants has also been beneficial by both providing ComReg with a wider European view and time to develop a significant detailed model.

Q. 10. Do you agree that the fault clearance charge should remain a separate charge from the LLU monthly rental charge? Please state the reasons for your response.

BT Response 10

BT considers that LLU rental should be normalised and the maintenance charge should be included in the rental charges particularly as the line fault index is so high and LLU operators are required to pay for repair on a per incident basis, unlike other eircom services. I.e there is no incentive on eircom to improve its repair service as it does not experience the cost within the product.

BT can and does provide test data to eircom and can provide the same test results as eircom use themselves. BT is aware that the other LLU providers also have facilities to provide test information diagnostics.

The eircom ARO price list acknowledges that operators can provide the test information, and given this acknowledgement the line rental should include maintenance where the test information is provided. **Hence where test results are supplied there should be no separate charge but a different monthly rental.**

BT notes that in the UK, BT offers the full Unbundling for £7.20 (equals 8.29Euro) per month and this includes the automated remote test facility and line maintenance. The UK circuits are also copper based with an infrastructure similar to that of eircom's access network. See Table 1 below for the rental prices.

Table 1 Monthly Rental Comparison between UK and RoI Full LLU.

	Monthly Rental in Euro exVat
ULMP - Full LLU Monthly Rental. 117 Euro to dispatch an engineer to test the line manually.	16.43
UK Full LLU Monthly Rental – remote automated test facility used.	8.29 Euro as at 10/06/09

See Annex A for a full list of charges in Europe taken over a three year period where Ireland provides the highest price rental in Europe.

Q. 11. Do you agree that exchanges with working lines in excess of 1,600 is a reasonable cut-off for those exchanges that are unlikely to be economically viable for OAOs to unbundle in the timeframe of the proposed price control period? Please state the reasons for your response.

BT Response 11

BT believes that exchanges with working lines in excess of 1600 lines is a reasonable cut-off to distinguish between those exchanges where is viable for OAOs to unbundle in the timeframe of the proposed price control. BT is of the view that it is highly unlikely it would unbundle at an exchange in Ireland with less than 1600 given the economics of trying to recover the costs. For example, if an operator were to assume it would achieve a 10% market share in an exchange area with 1000 lines, which would be very optimistic given eircoms dominance (circa 80%) of the retail market, the best it could expect is 100 customers. In the consumer market is would not be possible to recover the backhaul; equipment costs and running costs etc to make such an investment viable.

Q. 12. Do you agree that it is unlikely that an OAO would unbundled a line unless it was able to provide broadband services over that line; and do you agree that 5km represents the maximum line-length that may be used for those services? Please state the reasons for your response.

BT Response 12

BT agrees that it is unlikely that an OAO would unbundle a line unless it was able to provide broadband services over that line. To recover the investment and running costs OAOs need to offer a package of services to customers to achieve a sufficient return on investment. To limit the offering to voice would not provide a sufficient return and other markets characteristics such as churn show that bundles are subject to less churn than single services.

On the issue of whether 5Km represents the maximum line length that is used for broadband services BT would agree that this is the point where the line quality is likely to degrade rapidly for the lines in Ireland and commercial offerings become difficult. BT agrees with ComReg's reasoning at this time, however, given that technology keeps advancing an improved solution could appear at some time in the future to increase the workable distance. At this time 5Km is a reasonable distance for the foreseeable future and period of this review given the technology deployed and available in the market,

Q. 13. Do you agree that ComReg's proposal is conservative in that it includes an element of the costs associated with lines in excess of 5km?

BT Response 13

BT agrees that ComReg's proposal is conservative by including an element of the costs associated with lines in excess of 5km is reasonable as these will have a small impact on the exchange area costs.

Q. 14. Do you agree with ComReg's proposed weightings, as set out above, used in relation to the cost associated with long lines and small exchanges? Please state the reasons for your response.

BT Response 14

BT agrees with ComRegs's proposed weightings for the cost associated with long lines and small exchanges as this offers a fair balance between the incumbent recovering its costs and the LLU operators not being hit by costs not required.

Q. 15. Do you agree that the charge at option 4 is the most appropriate charge for setting the LLU monthly rental charge going forward? Please state reasons for your response.

BT Response 15

BT agrees that Option 4 is the appropriate methodology for setting the LLU monthly rental charges for Ireland; however BT considers that the proposed value of 12.12 Euro is far too high for the following reasons.

- The 12.12 Euro line rental needs to be qualified that it does not include maintenance hence is in reality only a part charge. Given the poor state of the eircom access network BT observes that it would have to pay an additional repair charge per year and this will provide the 'net' rental per customer. If as detailed in clause 4.130 of the ComReg consultation the Line Fault Index is 12.5% this would mean that each line has a 12.5% probability of going faulty each year. This would have a cost implication of 12.5% multiplied by 117 Euro or 109.7 Euro (the eircom price per repair) per year per line. I.e. an additional charge per month on each line of either 1.22Euro or 1.14Euro depending on the fault order type used. Hence the headline price is more realistically 12.12+1.14 = 13.26 Euro per month.

- Other countries appear able to hit significantly lower prices of around 8.29 Euro per month for LLU line rental with repair charges included. At 13.26 Euro per month Ireland is still out of kilter with Europe.

- BT is of the view that the proposed price minus the maintenance charge is of little value and will not address the competition issue in this market. BT considers that the cost saving announced by eircom should be factored into the cost model and assuming these will be in the order of 25% given headcount reductions, closing costly buildings etc, (see question 6) the reasonable and fair LLU monthly rental price would be in the order of 25% multiplied by 13.26 Euro which would equate to an LLU line rental price of 9.95 Euros per month including repair.

- For LLU eircom will recover its costs immediately as the network is already in place and the supply of LLU services are already available.

- Isolating housing costing approach. - A common reason put forward by eircom for higher rental prices is the high level of standalone houses in Ireland. BT considers that the boom of the last fifteen years has changed this situation (if it ever existed) as the large majority of new housing is in the form of estates rather than isolated houses, and most people in Ireland live in the cities or housing developments rather than in isolated houses. Urban planning rules also now require underground feeds to new houses rather than overhead drop wires. BT therefore considers that it is eircom's inefficiency and costing approach that is leading to high costs rather than the costs of serving isolated houses. Using ComReg own analysis of under 1600 line exchanges, LLU is unlikely to address the rural areas and thus LLU is more appropriate to urban areas and customers would be served by underground cables.

- Inefficient services – Whilst eircom continue to support dual systems for its own downstream provider and separately for the OAOs they are making the conscience decision to be inefficient. Regulation is aimed at encouraging efficient operators and for this reason ComReg should only allow eircom to recover such costs it would reasonably require to run single provision and assurance platforms that would offer equivalence of Input to all downstream providers including its own downstream provider. Eircom has had many years to have offered the same to all and have not taken this opportunity, preferring to continue what we believe is a discriminatory approach. ComReg need to act now by providing cost recovery that creates the correct incentive for efficiency. This discrimination is brought out very clearly as year on year LLU Line Share prices have increased, yet eircoms own bitstream service that uses the same input as line share llu has constantly decreased in price. The discrimination needs to be addressed through the cost models and regulating for efficiency.

In conclusion BT considers that Comreg should be looking at a full unbundling rental price of 9.95 Euros rather than over 13. Euros.

Q. 16. Do you agree that the charge at option 2 results in the most appropriate charge for setting the SLU monthly rental charge going forward? Please state the reasons for your response.

BT Response 16

Whilst BT does not see SLU being deployed other than for very exceptional circumstances due to the very small prospective customer base vs. high costs of setting up, BT does agree that Option 2 is the appropriate charge for setting SLU monthly rental charges going forward.

Q. 17. Do you believe that given the current economic circumstances that a proposed price control period of three years with a review in year 2 is the most prudent option? Please state the reasons for your response.

BT Response 17

BT believes that the previous price control period was far too long and allowed LLU pricing to become detached from reality and unreasonably kept LLU pricing high which in turn has directly led to the poor take up in Ireland. However, BT also believes that too short a price control period (say2 year) would remove confidence to invest. BT therefore agrees that three years, even in the current economic conditions is an appropriate length of time for this price control period. The safeguard of setting a time limit of two yeas for a new review is prudent as the previous price control period has proven to be far too long.

Q. 18. Do you believe that the draft direction is clear, precise, and intelligible from a legal, technical and drafting perspective? Please state the reasons for your response.

BT Response 18

BT considers that the direction needs to be re-drafted to include all the operators in the market, and specifically it should be modified to included the largest player in the market, i.e. eircom Retail as a downstream provider. Without such a modification their will be no transparency of what eircom are offering themselves, we believe their will be potential for eircom to discriminate against OAOs, the market will continue on its route foreclosure and it will continue to be difficult for ComReg to address margin squeeze and discrimination issues.

Q. 19. Respondents are invited to comment on the draft direction from a legal, technical and drafting perspective as set out above.

BT Response 19

BT observes that eircom offers to itself both LLU (ULMP) and Line Share services as components for its own downstream products. For example:

- WLR uses the ULMP as an input.
- EULs in PPCs and leased lines are based on the ULMP input.
- Bitsream is based on the LLU Line share product.

BT notes that eircom is regulated through ComReg Decision D8/04 which states:

(Italics added)
6 OBLIGATION OF NON-DISCRIMINATION
6.1 eircom shall have an obligation of non-discrimination as provided for by Regulation 11 of the Access Regulations.

6.2 Without prejudice to the generality of section 6.1, eircom shall apply equivalent conditions in equivalent circumstances to other authorised undertakings providing equivalent services and shall provide services and information to others under the same conditions and of the same quality as eircom provides for its own services or those of its subsidiaries or partners.

BT considers that eircom is not applying equivalent conditions in equivalent circumstances as eircom use the same copper access facility for themselves as for other operators as observed by customers being able change from eircom to an OAO and visa versa. However the charges and service features available for downstream eircom services such as bitstream suggests eircom are receiving both different facilities and access charges.

BT considers that as the physical access facility is the same for both eircom and the OAOs, eircom must offer to the industry exactly the same service as its offers itself. BT has itself proven through its OpenReach provider that this is possible and so does not accept eiroms arguments that its not. As companies cannot offer contracts to themselves eircom must publish an Internal Reference Offer (IRO) (which is not a contract) which should be the same as the ARO offered to other providers. Eircom must then use the same inputs, terms, conditions, slas, and prices as the rest of industry. BT is confident this will lead to a significant improvement in service quality through the internal incentives it will drive within eircom. See Annex B for suggested changes to the Draft Decision

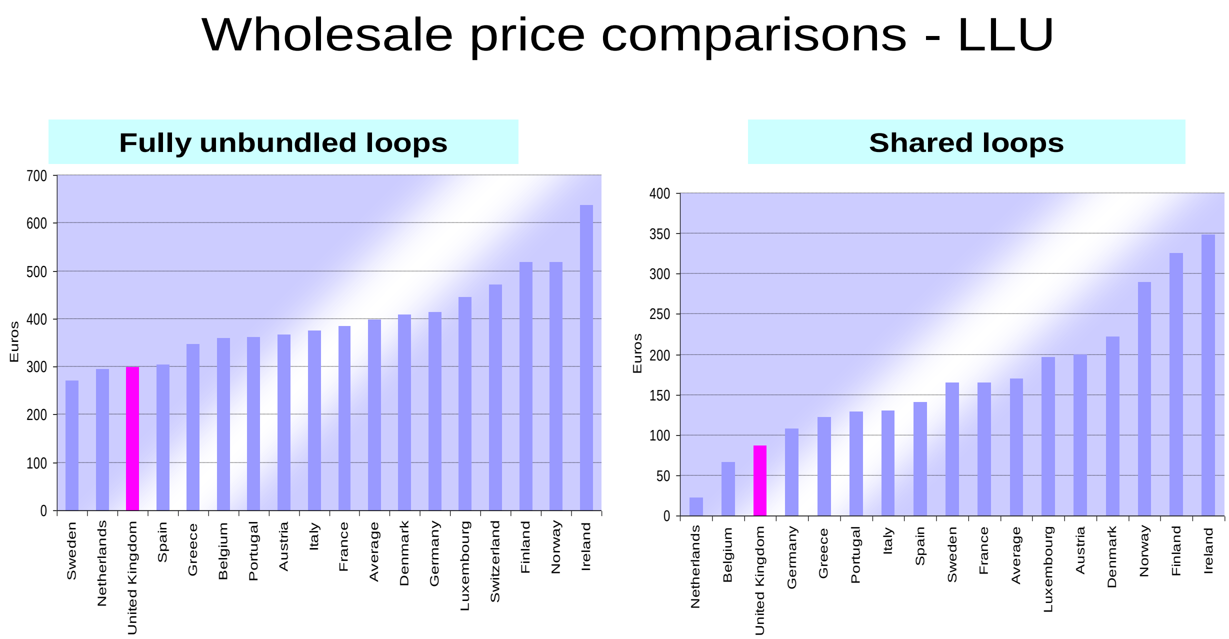
Q. 20. Respondents are requested to provide views (if any) which ComReg should consider in completing its Regulatory Impact Assessment.

BT Response 20

BT would like to make the following comments.

- Model – BT is disappointed that it was not afforded the same opportunity to have studied the costing model as was provided to eircom. BT has a considerable amount of expertise in LLU within its organisation and could have offered constructive comments based on experience of providing over 5 million LLU lines in other jurisdictions including the UK and Italy. BT is of the view going forward that any such future models should either be provided to no operator or to all interested parties.
- Option 3 – BT agrees with ComReg that option 3 provides the greatest net benefit and should be applied.
- Maintenance Charge and LLU Line Rental. BT remains of the view that work is required to normalise the maintenance arrangement and believes that Maintenance should be covered in the model.
- BT is therefore of the view that the proposed monthly rental price of 12.12 Euro is still over-recovering eiroms costs and the price should be closer to 9.95 Euros per monthly including line maintenance.

Annex A The high price of LLU in Ireland (3 Year price Comparison)



exchange rates at 24 March 2009

Annex B Suggested changes to the Draft Decision

6 Draft Decision

1 STATUTORY AND LEGAL POWERS

1.1 This Direction is made by ComReg, pursuant to the following:
i. Section 10 of the Act of 2002;
ii. Regulation 10 (5) of the Access Regulations;
iii. Regulation 14 (4) of the Access Regulations;
iv. Regulation 15 (2) of the Access Regulations;
v. Regulation 17 of the Access Regulations; and
vi. The SMP Decision, in particular, but not limited to, sections 3, 9 and 13 thereof.
1.2 This Direction is also made by ComReg having regard to and having taken in to account the following:

i. Section 12 of the Act of 2002;
ii. Regulation 14 of the Access Regulations;
iii. The Policy Directions made by the Minister for Communications, Marine and Natural Resources on 21 February, 2003 and 26 March 2004;
iv. The submissions received in relation to ComReg Document No.08/56, ComReg Document No.09/39 and ComReg Document No. [●] ;
v. The analysis and reasoning set out in ComReg Document No. 08/56, ComReg Document No. 09/39 and ComReg Document No. [●] which shall, where necessary, be construed together with this Direction; and
vi. The Model, which shall, where necessary, be construed together with this Direction.

2 DEFINITIONS

2.1 In this Direction:

"Access Regulations" means the European Communities (Electronic Communications
Networks and Services) (Access) Regulations 2003, as amended by the European Communities (Electronic Communications Networks and Services) (Access) (Amendment)
Regulations 2007 and as at any time subsequently amended;

Response to Consultation Document No. 08/56 & Further Consultation on LLU
& SLU Monthly Rental Charges
76 ComReg 09/39

"Act of 2002" means the Communications Regulation Act, 2002 as amended by the
Communications Regulation (Amendment) Act, 2007 and as at any time subsequently
amended;

"ARO" means the most up to date version of the Access Reference Offer published by
Eircom;

"IRO" means the most up to date version of the Internal Reference Offer published by eircom of services it offers to is own organisation.

"ComReg" means the Commission for Communications Regulation, as established under
section 6 of the Act of 2002;

"ComReg Decision No. D15/04" means ComReg Decision No. D15/04 entitled *"Decision
Notice and Direction – Local Loop Unbundling: Review of Eircom's ULMP Monthly
Rental Charge",* dated 5 November 2004 (Document No. 04/110);

"ComReg Document No. 08/56" means ComReg Document No. 08/56 entitled *"Consultation - Proposals for Local Loop Unbundling Pricing Methodologies",* dated 10
July 2008;

“ComReg Document No. [●]” means [●];
“Eircom” means Eircom Limited and its successors and assigns;
“LLU” means local loop unbundling;
“Model” means the costing model, developed by ComReg (in consultation with Eircom)
for the purpose of deriving the price of LLU and SLU, which has all necessary legal effect,
including but not limited to the purpose of determining cost orientation and Eircom’s
compliance with its obligation of cost orientation under section 9 of the SMP Decision;
“OAO” means other authorised operator;
“EIDP” eircom intenal downstream provider
“SLU” means sub-loop unbundling; and
“SMP Decision” means ComReg Decision No. D8/04, entitled *“Designation of SMP and*
SMP Obligations - Market Analysis: Wholesale unbundled access (including shared
access) to metallic loops and sub-loops”, dated 15 June 2004 (Document No: 04/70).

3 SCOPE AND APPLICATION

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

4 REVISED LLU AND SLU PRICES

4.1 Eircom is hereby directed to charge no more than the following prices for LLU and SLU, as derived from the Model:
i. LLU – € [●] per line per month; and
ii. SLU – € [●] per line per month.
4.2 Section 4.1 shall apply to all relevant invoices issued by Eircom to OAOs in respect of LLU or SLU, 30 days after the effective date and to all relevant invoices issued by Eircom to OAOs in respect of LLU or SLU at any time thereafter.

5 PUBLICATION OF PRICES IN THE ARO and IRO

5.1 The prices referred to in section 4.1 shall be in substitution for the prices for LLU
and SLU, as currently published in the Access Reference Offer (“ARO”). New prices shall be published in the eircom IRO.
5.2 Eircom shall publish the revised prices for LLU and SLU referred to in section 4.1, in its ARO and IRO and on its wholesale website, 30 days after the effective date.

6 REVOCATION OF COMREG DECISION NO. D15/04

6.1 Subject to section 6.2, ComReg Decision No. D15/04 is hereby revoked, 30 days
after the effective date.
6.2 Section 6.1 shall not come in to operation if this Direction is appealed, or otherwise the subject of legal proceedings and if a stay or suspension in respect of this
Direction (or a section or provision or portion of this Direction) has been ordered by a Court, or if this Direction (or a section or provision or portion of this Direction) is quashed or found unlawful or invalid by a Court, or remitted by a Court to ComReg.

7 SEVERANCE AND MAINTENACE OF PROVISIONS

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

8 STATUTORY POWERS NOT AFFECTED

8.1 For the avoidance of doubt, 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 on or prior to or after the effective date of this Direction) from time to time as the occasion requires.
8.2 Without prejudice to section 8.1, ComReg may, at its sole discretion, review and if it considers necessary, amend, continue in force, replace, or revoke this Direction
or the Model (or both) whether in whole or in part, in particular, if exceptional circumstances arise. Exceptional circumstances may include, but are not limited to the following: significant changes in underlying costs or price trends or significant changes in working line volumes.

9 EFFECTIVE DATE

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

5 Magnet Networks Ltd.

Introduction

Overall, Magnet Networks welcomes the proposed price reduction but is disappointed at the extent of the reduction and also the overall price review findings on which it is based.

Price Proposal

Magnet welcomes the proposed move towards reflecting the reality that not all lines will be unbundled and therefore cost recovery should only be based on those lines most likely to be unbundled.

Magnet is however disappointed that the proposed pricing, even with restricted costs recovery is still high. Magnet was expecting a price reduction to around €10 per line based on European averages and more importantly based on countries with equivalent demographics to Ireland. Even with the proposed price reduction Ireland would remain as the 4th most expensive in Europe.

Magnet would propose that a further reduction in the number of exchanges reasonably likely to be unbundled would bring the pricing closer to the European norms and stimulate greater competition through encouraging further unbundling.

Model

Magnet Networks is truly amazed that after such extensive research and modelling with inputs from external consultants and industry that the costs of building an efficient network from the bottom up resulted in a price which differed by only 9 cent from pricing which has been based historically on cost inputs from eircom. Since the publication of the proposal eircom has finalized details of a significant costs reduction plan with more to follow also of note are deflation figures for Ireland have been confirmed at approx 3.5% for 2009 YTD. We feel that this can further feed in to a price reduction.

We believe the long:short line weighting ratio is disproportionate and needs to be adjusted.

We believe a more aggressive and practical approach is required to drive investment in LLU and attract new investment.

Consultation Questions

Q. 1. Do you agree that the period from 2000 to 2012 is a reasonable length of time to evaluate the price trend data for the copper access network assets? Please state the reasons for your response.

Magnet Networks agree a 12 year period is a reasonable length of time to evaluate the price trend of copper in light of the copper access network asset. However, the period chosen is one of the highest CPI'ed period in the history of the state. Thus, Magnet Networks suggest that a longer and more historic look at copper price trends should take place taking into account the rate of inflation in the last ten years.

Magnet Networks do not believe that the weighting at section 4.48 goes far enough to reflect current realities. The ESRI has indicated unemployment rates of up to 16.8%[1] by the end of 2010 causing a dramatic lowering of labour rates and associated benefits. Indeed many are predicting a period of up to ten years or more to see employment levels return to 2007 levels and longer for standards and rates of pay.

Magnet Networks also notes that CPI for 2009 is likely to be negative to the tune of 3.5% given recent announcements on CPI. "Services" for the period were running at negative 3.2%.

In this regard, and to reflect reality, we believe that the 2008-2012 period should have a factor weighting of an additional 50%. As BU-LRAIC models are forward looking (not regressive) this also matches the time frame to the model.

Fig 1 – CPI& HICP –CSO

Consumer Price Index
April 2009

CPI and HICP

	CPI		HICP	
	% monthly change	% annual change	% monthly change	% annual change
Dec 2008	- 1.2	+ 1.1	- 0.7	+ 1.3
Jan 2009	- 1.7	- 0.1	- 0.8	+ 1.1
Feb 2009	- 0.4	- 1.7	+ 0.2	+ 0.1
Mar 2009	-	- 2.6	+ 0.1	- 0.7
Apr 2009	- 0.8	- 3.5	+ 0.1	- 0.7

Q. 2. Do you agree that the basis used for forecasting price trends for copper and the other local loop assets (i.e. poles, trenches, chambers, MDFs, street cabinets, etc) appears reasonable? Please state the reasons for your response.

Magnet Networks agrees with ComReg's methodology but does not believe that the assumptions used in copper pricing are correct.

As industrial output falls, commodity pricing reacts accordingly. Metals such as copper and Zinc are sensitive to economic activity and as can be seen in copper

[1] http://www.esri.ie/publications/latest_publications/view/index.xml?id=2738

mines (Rio Tinto et al) in copper producing countries, demand is falling while there is a growing over supply. In the commodity market, this causes prices to drop.

The gains shown in recent months are short lived and fuelled mainly by restocking in China, which is a finite exercise. In recent weeks, fluctuations are now again being experienced and reflected in the LME.

Analysts say copper faced weakness in coming months as supportive buying from China tails off and ahead of a seasonally quiet market period.

"The buying spree that China went on in the first half of the year is going to be very difficult to sustain because it was largely fuelled by restocking, which is a finite process," said Gayle Berry, metals analyst at Barclays Capital in London *(May 2009)*

"As a result we're going to see imports fall back over the next few months which, together with a seasonally weaker period for northern hemisphere demand, and continued concerns on the macro front, means it's going to be a tough couple of months for metal prices."[2]

Over the past 3 years copper prices dropped dramatically from an output peak in 2006 & 2007 to levels seen in 2005. The 3 year pricing trend is declining for each year in question.

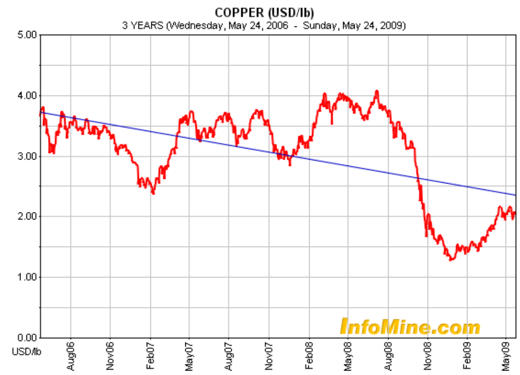
Fig 2 – Copper pricing trends – 1, 2 & 3 year view- infomine[3]

1 year trend 2 year trend

3 year trend

[2] http://www.businessworld.ie/livenews.htm?a=2421879

[3] http://www.infomine.com/Investment/HistoricalCharts/ShowCharts.asp?c=copper



On May 20, 2009, the International Copper Study Group's (ICSG[4]) preliminary data showed that world copper production outpaced refined usage by 86,000 tons in the first two months of 2009, compared to a production deficit of 61,000 tons the previous year.

So far in 2009, world refined production is up slightly while refined usage is down 4%. In 2008, world refined production exceeded consumption by 234,000 tons. On April 21, 2009, **the ICSG predicted that copper will show a world production surplus of 345,000 tons in 2009 and 418,000 tons in 2010**.

This over production, coupled with existing drops in prices will keep copper prices steady or declining for several years to come with an upward sustainable recovery only expected[5] approaching 2013, i.e. the period of the next review but not this one.

Equally we believe that the inflation seen in the costs of civil works for trenches, chambers and digs has returned to that seen in prior to the construction boom years and is now downward.

We would also bring ComReg's attention to recent reductions in energy pricing and the likelihood of the CER further reducing energy prices later in 2009 and 2010.[6]

Magnet Networks acknowledges ComReg's hard work and time that has gone into this consultation, however, it should be noted that the economy is in free fall with

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4 http://www.icsg.org/index.php?option=com_docman&task=cat_view&gid=13&Itemid=61

5 http://www.theaustralian.news.com.au/business/story/0,28124,25540822-36418,00.html

6 http://www.cer.ie/en/information-centre-newsletters.aspx

labour costs, energy costs, contractor costs thus, this should all feed into a lower future pricing of LLU. It should also be noted that this consultation is long overdue.

Q. 3. Do you agree that it is reasonable to consider that contractor costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

Magnet Networks agree that contractor's costs will decrease over the next 3 year period by approximately 50% due to lower volumes of work and therefore more competitive tendering, and also reductions in input costs including labour and materials.

Q. 4. Do you believe that the volumes of working lines will increase, decrease or remain static over the proposed price control period? Please state in percentage (%) terms your views on the likely movements with detailed calculations, if necessary.

Magnet Networks believes the number of working lines will essentially static due to low build forecasts, move to cable providers and an overall household policy of saving money precipitating a move to mobile above fixed lines.

Q. 5. Do you agree with ComReg's preliminary view that working capital should not be included in the BU-LRAIC cost model used to determine the LLU monthly rental charge? Please state the reasons for your response.

Magnet agrees that due to the difficulty of obtaining a true value of working capital thus including it would be a misrepresentation of the LLU price.

Q. 6. Do you agree that it is reasonable to consider that labour costs will reduce over the proposed three year price control period? Please state the percentage (%) which you expect labour costs to reduce over this period.

Yes we believe roughly one third due to downward pressure on labour hire costs arising from high unemployment especially in the construction market. Currently, businesses have requested employees to take a 10% -20% reduction in current salary and if hiring are offering significantly less to future employees.

Q. 7. Do you agree that the LFI of the current Eircom network is not an appropriate basis on which to set the operating costs of a BU-LRAIC model in determining the LLU and SLU monthly rental charge? Please state the reasons for your response.

Magnet agree with ComReg as the LFI in most cases relates to a legacy network built many years ago and therefore it is not appropriate to have it included.

Q. 8. Do you agree that the LFI of an efficient BU-LRAIC model, used to determine the LLU and SLU monthly rental charge, should be based on an LFI not exceeding 8%? Please state the reasons for your response.

Magnet Networks agrees with the methodology but view this final capped number as far too high.

The World Bank in it's guidance on "QUANTITATIVE INDICATORS FOR QUALITY OF SERVICE" states

"7.2 The number of faults per main line per year defines the frequency of breakdown of the telephone lines. For a well constructed and well maintained network, the **average number of faults per main line per year should be 0.2 or less**; that is the telephone line should not be out of order more than once in five years. Because the figure is normally small in industrialized countries, this indicator is often expressed in faults per 100 main lines. The actual situation in developing countries is much worse, with the average number of faults in some countries exceeding three faults per main line per year.[7]

Currently the World Bank in 2006 has assessed that line faults in Ireland were 3.2 per 100 lines[8] thus allowing the incumbent a higher line fault permissible threshold is not acceptable. An acceptable LFI for moving forward would be 1%. Ireland needs to return to a situation where faults are not tolerated and where the network has excellent preventative and reactive maintenance performed. While USO penalties will go some way to addressing this we need to strive to a "zero fault" rate as best in class. While "zero faults" is not realistic in practical terms it needs to be a goal.

A high LFI will lead to dissatisfied consumers. This is not a positive outcome.

Also as LLU is most likely to occur in urban areas, the LFI should tend to the lower end of the scale.

Q. 9. Do you agree with the overall preliminary approach taken by ComReg above in relation to the basis used in determining the capital costs and operating costs used in the BU-LRAIC model for determining the monthly rental charges of LLU and SLU services in Ireland? Please state the reasons for your response.
Magnet Networks agree with the principles outlined but as no figures or %s were provided it is impossible for us to make a meaningful assessment.

In general we note the level of prior exposure of costs models, principles etc that was afforded to *eircom* (or so it appears) in arriving at many of the conclusions

[7] http://www.worldbank.org/html/opr/pmi/telecom/teleco01.html

[8] http://devdata.worldbank.org/ict/irl_ict.pdf

outlined. While we fully understand and accept that there is a level of practical work that needs to be done, OAOs have had no exposure what so ever to maps, GIS information, models etc quoted by ComReg. While we are not critical of this it is noteworthy, especially when the output from the model in terms of proposed line rental with full recovery was only 9cent different to outputs based on the historical eircom provided model

Q. 10. Do you agree that the fault clearance charge should remain a separate charge from the LLU monthly rental charge? Please state the reasons for your response.

In the bistream market line faults are not a separate charge to the wholesale bitstream price thus, Magnet Networks suggest that line faults should not be a separate charge to the wholesale LLU price. A separate fault charge leads to an over recovery of costs as maintenance and engineers staff if they are also included in the cost of the network. Magnet does not have access to the model to verify Magnet Networks believe having a fault inclusive LLU monthly rental charge would ensure that lines are maintained to a high quality and prevent the over recovery of costs.

Q. 11. Do you agree that exchanges with working lines in excess of 1,600 is a reasonable cut-off for those exchanges that are unlikely to be economically viable for OAOs to unbundle in the timeframe of the proposed price control period? Please state the reasons for your response.

Magnet Networks agrees with the methodology but we believe this selected figure to be too low for this period of the review. A number close to 5,000+ lines for the initial period of the control would be far more reflective of what is likely to happen in the period. As LLU progresses and exchanges are unbundled a more graduated control (Glide path) can be applied but it is essential to kick start investment now and keep costs high at this point is unwise and will not have the desired impact. OfCom have introduced glide path pricing for LLU pricing.[9]

Based the number of lines per exchange Magnet has determined that extending the number of exchanges to those with 1500 lines from those with 5000 lines has the following impact:

- Total number of lines increases from approximately 947,000 to 1,332,000 – a 41% increase
- Total number of exchanges increases from 96 to 239 – a 141% increase.

[9] http://www.ofcom.org.uk/consult/condocs/openreachframework/statement/statement.pdf

Assuming that the number of exchanges has a larger impact on the cost inputs, the inclusion of exchanges up to 1500 has a disproportionate impact on costs relative to the number of lines.
While there is always a question in relation to urban and regional divide – including more regional MDFs is simply artificially keep the line price high for all lines. This will reduce the likelihood of investment taking place and will not attract new entrants to the market. In this situation no one wins, urban or rural. Magnet suggest that a larger minimum point is selected (5000 lines) for the period of this review or that a glide path approach is adopted to match real uptake to costs of provision. Investment and competition must be encouraged at all costs as this ultimately drives consumer benefit.

An alternative method would be to provide a glide path for each year of the control based on the number of smaller and larger exchanges actually unbundled in that period as opposed to front loading costs at this point even though it is highly unlikely that unbundling of small MDFs will take place at all in the initial period of the control. This can be expressed as a planning ratio or as a hard number.

Q. 12. Do you agree that it is unlikely that an OAO would unbundled a line unless it was able to provide broadband services over that line; and do you agree that 5km represents the maximum line-length that may be used for those services? Please state the reasons for your response.

An OAO would not unbundle a line with only PSTN on it. However, overall we are in agreement with the 5km maximum length.

Q. 13. Do you agree that ComReg's proposal is conservative in that it includes an element of the costs associated with lines in excess of 5km?

Yes Comreg's proposal is extremely conservative but Magnet don't understand why ComReg still insist on including costs for lines greater than 5km as that is rewarding an inefficient operator and penalising the customer. A more aggressive approach is required and now is not the time to be overly conservative – LLU has failed in Ireland for ten years, extending this is neither wise nor desirable for consumers or industry.

We again come back to the point that as a nation we need to urgently attract investment and new entrants into the Irish market and attract renewed take up of PSTN based services.

Q. 14. Do you agree with ComReg's proposed weightings, as set out above, used in relation to the cost associated with long lines and small exchanges? Please state the reasons for your response.

Magnet Networks supports the logic and methodology but we do not support the proposed weighting ratio. While Magnet believes the weighting may become relevant in the future, we feel the initial period of review is not the time to implement this to the full extent.

While we do not disagree with the logic and similarities with France, we would like to remind ComReg of the position of LLU in Ireland today.

- Ireland are many years behind France, we need an incentive to rapidly drive LLU.
- There are 57 unbundled exchanges in Ireland despite LLU being available for many years
- The current economic conditions will state that LLU, rightly or wrongly, will only happen in urban areas/larger exchanges for the immediate term
- Line price will drive LLU and attract new market entrants
- LLU has failed in Ireland for ten years and rapid remedial action is required to drive demand and gain traction on the ladder of investment towards NGN

It is very important to remember that regardless of the "rights or wrongs" of the rural and urban divide it is true to say that if the LLU price is not at a level to attract new investment at all then neither demographics will benefit. You already acknowledged this in later comments on SLU.

As with exchange sizes, we believe that the most important thing now is to gain investment in LLU. At the point of the next pricing review (3 years) ComReg should then look to include the proposed weightings if LLU has been deployed in urban areas, as would be expected and expansion to smaller MDFs is then more likely. Again, we suggest the approach of a glide path.

We are however mindful of exchanges in rural areas and the need for some degree of recognition that it is possible, at least in theory, that some very limited rural exchanges may be unbundled as a result of grant aiding etc. We also acknowledge that some longer lines do exist within urban exchanges. With this in mind we would recommend a 99:1 ratio to be used at maximum for the period of this review.

This answer should also be read in conjunction with the answer on exchange sizes and perhaps again a glide path based on actual rollout would be more appropriate.

Q. 15. Do you agree that the charge at option 4 is the most appropriate charge for setting the LLU monthly rental charge going forward? Please state reasons for your response.

Of the options that ComReg have published in this consultation, option 4 is the lowest price and thus, the most appropriate option but not the most appropriate charge. This option along with all the other options laid out in the consultation fail and will continue to fail to encourage investment in LLU in Ireland. As the largest LLU provider in Ireland we will not unbundle any more exchanges at the proposed price as it is still an unattractive investment. We encourage ComReg to seek a deal similar to the Ofcom/BT agreement of 2005 relation to LLU and non movement on bitstream prices. There is already a squeeze on the low end LLU products i.e. 1mb and 3mb by bitstream and this is moving further up the speed ladder to LLU's detriment.

Magnet overall agree with the mechanism and logic but disagree with the calculated price due to:-

- The weighting factor
- The exchange size and exclusions

Magnet also reiterates earlier comments that we were surprised that an independent rebuilding of an efficient network from the bottom up resulted in similar costs and figures to that of the incumbent.

If the 99:1 weighting is adopted, the smaller exchanges are excluded, eircom's revised cost base is taken into account, the likelihood of reduced labour and contractor rates, deflation & copper pricing trends are followed, Magnet would hope a sub €7 rentalcharge would be achieved.

Q. 16. Do you agree that the charge at option 2 results in the most appropriate charge for setting the SLU monthly rental charge going forward? Please state the reasons for your response.

Agree.

Q. 17. Do you believe that given the current economic circumstances that a proposed price control period of three years with a review in year 2 is the most prudent option? Please state the reasons for your response.

Agree.

Q. 18. Do you believe that the draft direction is clear, precise, and intelligible from a legal, technical and drafting perspective? Please state the reasons for your response.

Agree.

Q. 19. Respondents are invited to comment on the draft direction from a legal,

technical and drafting perspective as set out above.

Agree.

Q. 20. Respondents are requested to provide views (if any) which ComReg should consider in completing its Regulatory Impact Assessment.

Agree.

Conclusion.

Magnet welcome the consultation, however, as we have not seen the inputs bar at a generic high level thus we do not have a full understanding how the options were reached. Again, we are concerned about the similarities between eircoms costs and those that an 'independent' assessment arrived at.

Magnet also notes that the consultation on "ComReg 08/106 - Rental Price for shared access to the local loop" is still ongoing and no decision has been made, despite the consultation closing in February 2009. This decision is important to ensure the continued interest in LLU and to encourage competition. Also " ComReg 08/105 – Intra Migrations Premiums – Consultation and Draft Decision" decision is outstanding.

Magnet Networks cannot emphasise enough the importance of regulatory and pricing clarity to its ongoing business case. At this time Magnet has not built any price reductions into its forecasts in view of the slow rate of progress, and likely disappointment with the outcome. The consequences of this lack of regulatory and pricing clarity are significant in an environment where all investment cases must compete more than ever for approval. At this time Magnet considers the UK market and specifically Northern Ireland as a more attractive market for investment in LLU.

Magnet Networks are always happy to assist ComReg in any queries or requests they may have.

6 ALTO

alto
alternative operators in the communications market

12 June 2009

Ms Caroline Jordan
Wholesale Division
Commission for Communications Regulation
Irish Life Centre
Lower Abbey St.
Dublin 1

Dear Caroline,

Further Consultation on Local Loop Unbundling – Monthly Rental Charges 09/39

ALTO broadly supports the work of ComReg in further consulting on monthly rental charges in respect of Local Loop Unbundling, - LLU, in Ireland.

Our members will be making bilateral submissions to ComReg where they provide LLU services or have direct interests in the future development of the market.

We remark that current, and future indicative cost/prices for LLU could be lower than where the market is today and where it may end up post the 09/39 review.

Continued focus and impetus from ComReg is still required, as well as specific regulatory reform of repair, provision of service, backhaul and pricing in the LLU market.

We trust that the above will be helpful to your deliberations.

Yours Sincerely

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Ronan Lupton,
ALTO – Alternative Telecom Operators