



Office of the Director of  
**Telecommunications  
Regulation**

## **Interconnection Rates in the Irish Telecommunications Sector**

Status report

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# 1 Introduction

The provision of interconnection on fair and efficient terms is widely recognised as an essential requirement for the creation of a competitive telecommunications market. Interconnection charges can account for a substantial proportion of operators' costs. It is therefore important that these charges are soundly derived and give proper economic signals to operators to guide their investment decisions.

Under Irish telecommunications law, which is in turn developed from European law, an operator who is designated as having significant market power ("SMP") is required to permit other licensed operators ("OLOs") to interconnect with its network. To facilitate this process, the SMP operator must publish a reference interconnect offer ("RIO") that sets out the terms and conditions for interconnection and the prices to be charged. The contents and production of the RIO are subject to statutory requirements, compliance with which is overseen by the Director of Telecommunications Regulation ("the Director") and her Office ("the ODTR"). In particular, an SMP operator must justify to the Director's satisfaction that the prices set are in accordance with legal requirements that notably include the need for these prices to be cost-oriented, non-discriminatory and transparent. If the Director is not satisfied that prices are properly justified, she may direct changes to be made. *eircom* is an operator designated as having SMP in the relevant market and is governed by the Interconnection Regulations.

The Director is now publishing this document to provide a status report to the market on the interconnection rates contained in *eircom*'s RIO, including an update on developments since the ODTR last communicated to the market on interconnection and a number of positions that the Director is adopting in order to move the market forward at this time.

The key positions and actions which are now being adopted include:

- The finalisation of interconnection rates for the period to 1 December 1999 (previously set on an interim basis prior to liberalisation);
- The introduction of new interim rates that will apply from 1 December 1999 to 31 March 2000;
- The opening of a new consultation on all matters in D12/99<sup>1</sup>.

In addition to this document, three other relevant documents are being published. These are:

- Document ODTR 00/14 which sets out the Director's position on the interim interconnection rates that applied to 1 December 1999 and the finalisation of rates for that period. In summary, the Director believes that *eircom*'s proposal to finalise rates at the interim level as previously set is justified and can be accepted.
- Document ODTR 00/15 considers rates which will apply from 1 December 1999 to 1 April 2000. *eircom* has proposed a reduction during this period which the Director considers acceptable as a pragmatic interim rate that is appropriate for use while further work continues on the various work streams on interconnection.
- Document ODTR 00/16 is a consultation document that seeks further views and representations on the issues covered in decision notice D12/99.

The Director recognises the work that all parties have put into the consideration of interconnection issues, including the responses and comments of all players to consultations to date and the considerable amount of effort that has been put into this work by *eircom*. Furthermore, the Director has been assisted in her analyses of these matters generally by a number of consultancy firms, including ICC, Nera and Europe Economics. The Director would like to thank all parties for their commitment and effort.

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<sup>1</sup> ODTR Document 99/54 "Telecom Eireann Reference Interconnection Offer, Decision Notice D12/99 and Report on the Consultation", September 1999

## 2 Background

Background information to this status report is set out in appendix 1 including the legislative background to the interconnection regime in Ireland, related ODTR documents and decisions on interconnection and some information on linking costs with interconnection rates.

## 3 Current status

### 3.1 Introduction

During 1999 the ODTR initiated a number of work streams which concentrated on examining *eircom*'s cost accounting system, costing information and other inputs that impact on *eircom*'s interconnection rates, including a methodology for calculating Long Run Incremental Costs and ongoing benchmarking of other operators. This work was designed to provide the Director with sufficient information to consider a justification by *eircom* of its interconnection rates which the Director expected to receive in October 1999. The Director intended to take a position on that justification in sufficient time for new rates to be presented to the market by 1 December 1999 - a date that had been communicated to all parties well in advance. The timetable on these workstreams has not been met for the following reasons:

1. *eircom* justification to ODTR of RIO rates: *eircom* was not in a position to provide a justification to the ODTR as required in October 1999 due to delays in gathering and finalising relevant costing information.
2. The production of *eircom*'s regulatory accounts and the auditing of those accounts was delayed by two months. In addition, the ODTR has not been in a position to accept those accounts to date and has raised a number of queries on them.
3. The production of a LRIC model which is dependent on inputs from *eircom* and other parties in the industry through an Industry Advisory Group ("IAG"); this project experienced delays, including delays in the receipt of information. It is noted that other countries are also experiencing delays in finalising LRIC
4. The Director's decision on a number of relevant matters in the RIO as published in Decision Notice D12/99 was challenged by *eircom*, resulting in the automatic suspension of the decision by operation of law.

Against the backdrop of these delays and complications, the ODTR and its advisers have continued to work on the information available and to meet with *eircom* on matters relating to rates and accounts in an effort to move the interconnection market forward. The Director is now taking a position on a number of proposals which will provide for the continued reduction of interconnection rates in the Irish market. These positions are set out in documents ODTR 00/14 and ODTR 00/15.

### 3.2 *eircom*'s Regulatory Accounts

Part of any justification that interconnection charges are cost-oriented are the separated regulatory accounts which *eircom* is obliged to prepare.

The format and content of these accounts were the subject of documents ODTR 99/35, ODTR 99/43, and ODTR 99/52 and were expected from *eircom* by the end August 1999. For a variety of reasons, *eircom* was not in a position to produce these until 29 October 1999 when they were published. PriceWaterhouseCoopers (*eircom*'s existing auditors, appointed to audit the separated accounts) expressed an opinion that the accounts were prepared in accordance with *eircom*'s accounting documents but expressed no opinion on the accuracy of the figures

themselves. ODTR has inspected the accounts in detail and has identified a number of concerns which have been brought to *eircom*'s attention. As a result, the ODTR has not yet accepted the accounts as being compliant with the decisions set out in ODTR 99/35 and ODTR 99/52. The Director expects that *eircom* will publish supplementary information very shortly and that full discharge can be given in the coming weeks. She will publish a further document on the matter at that time.

Any deficiency in a set of separated accounts can have serious implications for a determination on rates based on an analysis of these costs and the Director has taken all other relevant and available information into account when taking the positions referred to in documents

### **3.3 Long Run Incremental Costing ("LRIC")**

The Director is most anxious to move rapidly to the use of LRIC as the basis for determining interconnection rates. However, the Director has always recognised the need for complex modelling work to be undertaken before LRIC rates can be used as the main input to any such decision.

Having consulted widely, the Director adopted the following approach:

- The ODTR would develop a bottom up LRIC model by December 1999,
- The top down LRIC model that *eircom* proposed to develop should be produced by 1 June 2000
- Both models would then be reconciled, and
- An industry group (the IAG) was established to assist the Director with the development of the top down model and to review the approach and results of *eircom*'s forthcoming top-down model.

Notwithstanding the effort and co-operation of all parties, particularly those who have contributed a substantial amount of data for the model, there have been delays in collecting suitable data and project is behind schedule. In addition, the IAG has identified a number of areas which merit further attention. These concerns are being addressed but will take time to resolve. However, the Director remains firmly of the view that LRIC is the appropriate mechanism for determining rates in the future and considers that the difficulties encountered can be overcome in the near term. She expects that the bottom up LRIC model can be available for use by end April 2000.

## **4 Positions of the Director**

### **4.1 Periods under consideration**

Interim rates were set during November 1998 and have remained at the same level until now.

- ODTR 00/14 considers rates up to 1 December 1999. The Director intends to finalise the rates to 1 December 1999 and does not propose to review these rates further.
- ODTR 00/15 considers revised interim rates that will apply from 1 December 1999 to 31 March 2000.

The Director looks forward to receiving *eircom*'s proposals for interim rates for the period from 1 April 2000.

In the meantime the ODTR will continue its work on interconnection rates with a view to making an early decision on the appropriate level of interim rates, having regard to all information available.

## **4.2 Principles underlying Interconnection**

The Director is pleased that the current developments are in line with the general principle that interconnection rates should reduce over time for a variety of reasons and she expects that further work, including LRIC work, will continue this trend. However, for the reasons set out earlier in this paper, the Director considers that the current positions being adopted in this document and documents ODTR 00/14 and ODTR 00/15 do not set precedents on the underlying principles for calculating interconnection.

## **4.3 Services to be included**

The ODTR's review has initially concentrated on key conveyance rates (termination, origination and transit) as these represent the majority of the costs to operators.

Additional work is being carried out on charges for all other interconnection services, for example interconnection links and other costs such as Intelligent Network costs which are an increasingly important element of a modern telephony network. The ODTR expects to continue its work on these areas and notwithstanding any interim positions arrived at, expects *eircom* to be in a position to present and justify rates for the period from 1 April 2000 forward, including rates for these services. The Director will publish further documents communicating her position on other services in the near future.

# **5 New Developments**

In this section, the ODTR lists some of the developments in telecommunications market since the last consultation run by ODTR on these matters which interested parties may wish to address in their responses to the relevant elements of ODTR 00/16.

## **5.1 Retail gradients**

It has been brought to the ODTR's attention by *eircom* that its retail gradients are excessively steep compared to European norms and that it might be expected that such gradients might come into line with European norms over time. If this were to be the case, weekend rates would be closer to peak rates, and such new gradients would be likely to result in a relative increase in interconnection rates for weekend calls and a compensating decrease in peak rate charges in situations where all other factors are held to be equal.

## **5.2 Routing factors**

Routing factors are influenced by the mix or profile of traffic that a network is carrying. This profile is influenced by the development of competition and increasing levels of interconnection traffic from fixed (as opposed to mobile) operators. As a result forward looking routing factors are likely to mean adjustments to the balance between primary, tandem and double tandem (long and short) interconnection charges. Network roll out providing more points of interconnection are likely to generate a shift in emphasis of interconnection traffic from double tandem to primary conveyance. In addition, the ODTR believes that, in due course, to calls within Dublin may be more likely to use a single tandem rather than double tandem routing. Taken together, these developments should lead to a progressive reduction of the unit cost of conveyance via *eircom*'s fixed network.

## **5.3 Call set up charge**

The Director notes the rapid increase in internet traffic and the increasing proportion of overall traffic that is made up of internet calls. Internet calls have different call holding patterns from voice traffic and may be specifically affected by the absence or existence of two part charging. The Director also notes developments in the UK market on call set up, where Oftel has

concluded that two part charging interconnection arrangements for number translation service (NTS) calls would be appropriate in some circumstances<sup>2</sup>

#### **5.4 Different charges for call origination, call termination and transit**

The Irish interconnection regime has not differentiated between call origination and call termination charges and the Director has to date considered this appropriate in the early stages of development of competition. However, the Director notes that the European Commission has recently stated that "...call origination services, transit services and call termination services are likely to develop as different markets to which different rules apply"<sup>3</sup> and considers this an appropriate issue to consider as the market develops.

## **6 Next steps**

All interested parties are asked to respond to the issues in ODTR 00/16 in the timescale set out therein.

Comments will be analysed by the ODTR and the result of the consultation communicated to the market. The ODTR will also consider how to proceed on the matter of interim interconnection rates to apply from April 2000.

In the meantime, in accordance with the position set out in ODTR 00/15 in relation to interim rates for interconnection, *eircom* will present revised interim rates to apply for the period from 1 December 1999 to 31 March 2000 and all operators will be in a position to avail of these rates. Operators should contact *eircom* directly in relation to operational matters relating to these rates.

The Director also expects that during this period

- Issues related *eircom*'s separated accounts can be finalised (a separate document will be published)
- The ODTR will make further communication to the market on interconnection rates other than call origination and termination,
- the LRIC model being developed with the advice of the IAG will be finalised during April 2000,
- the reconciliation between the *eircom*'s top-down and the ODTR bottom up LRIC models will take place in June against the most up-to-date relevant accounting data available within *eircom*.

Interim rates will be reviewed and finalised when final information is available to the Director.

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<sup>2</sup> OFTEL's Statement on the Relationship between Interconnection Charges and Retail Prices for Number Translation Services (December 1999) <http://www.oftel.gov.uk/pricing/nts1299.htm>

<sup>3</sup> the 1999 Communications Review, COM(1999)539  
<http://linux.ispo.cec.be/infosoc/telecompolicy/review99/>

# APPENDIX 1: Background Information

## ***Legislative background***

EU and Irish legislation set out procedures for providing interconnection. The most important of these are the following:

- Directive 97/33/EC of the European Parliament and Council of 10 April 1997 on “a common framework for general authorisations and individual licences in the field of telecommunications service” (the “Interconnection Directive”);
- European Communities (Interconnection in Telecommunications) Regulations, 1998 (as amended) (SI No 15 of 1998) (the “Interconnection Regulations”), which transpose the Interconnection Directive into Irish law.

The Directive and Regulations place special obligations on an operator who is designated by the Director as having SMP. The essence of these obligations is:

- interconnection charges should follow the principles of transparency, non-discrimination and cost-orientation;
- the Director may direct an organisation to justify its charges and to adjust these charges where they are not in compliance with these principles;
- the “burden of proof” regarding justification lies on the organisation providing interconnection;
- a RIO set out in accordance with market needs shall be published and the Director may direct changes to this offer, where appropriate.

In addition, guidance from the European Union on interconnection and the setting of rates intended to help Member States realise the objectives of the Interconnection Directive is of relevance. Of particular note are the following:

- Commission Recommendation of 8 January 1998 on interconnection in a liberalised market, 98/195/EC, as amended by Commission Recommendation of 29 July 1998, 98/511/EC;
- Commission Recommendation of 8 April 1998 on Interconnection in a liberalised telecommunication market. Part 2: Accounting separation and cost accounting (Part 1 was published on 15 October 1997)
- Commission Recommendation of 24 November 1999 on Leased Lines Interconnection pricing in a liberalised telecommunications market, C(1999)3863.

## ***Linkages between costs and interconnection rates***

The linkages between costs and interconnection charges are complex. Examples of some of the issues to be considered include the following:

- whether to use historic costs, historic costs adjusted for modern equivalent assets and their current costs or forward looking costs;
- the period over which investments (capital expenditure) are recovered and the manner (depreciation and amortisation policy) in which recovery occurs;
- the revenue streams that are considered to contribute to the funding of particular investments or operating expenses;
- the way capital and operating costs which are not directly attributable to a single product

are allocated to the different products (including retail products);

- the extent to which cost-orientation should be based on the costs of a reasonably efficient operator and what constitutes efficiency;
- assumptions about the way call are actually, or would be efficiently, routed through the network (routing factors) and therefore the manner in which individual elements of equipment are used to deliver particular services;
- the way total costs are apportioned throughout the day (tariff gradients).

Cost-orientation is not a simple matter and there is often a variety of ways – each of which may have validity – of establishing a cost-oriented charge. Indeed, it is a very easy matter to manipulate an allocation assumption, a set of routing factors, or any other input assumption to change, possibly in a substantial way, the final ‘price’. There is, therefore, no single answer that will be recognised as being correct by all parties and the Director, in considering whether *eircom* has justified its interconnection charges seeks not only satisfy herself that the arithmetic is correct, but also considers the assumptions made – and the alternatives that could have been made – having regard to the principles set out in law as well as other consideration that might reasonably be taken into account.

### ***Related decisions and documents***

Prior to liberalisation, *eircom* (then Telecom Éireann) published a set of interconnection rates. These had been submitted to the Director and she felt that they were acceptable as interim rates. The Director’s views were set out in two documents on interconnection<sup>4</sup> which recognised that a number of matters warranted further consideration. These matters were considered in a number of consultations that occurred during 1999. Notable amongst these were:

- A consultation and decision notice on the introduction of Long Run Incremental Costs (LRIC) as a basis for calculating interconnection rates<sup>5 6</sup>.
- A number of consultations and decision notices relating to *eircom*’s separated accounts<sup>7 8</sup> and on costing methodologies<sup>9</sup>.
- A broad ranging consultation on the RIO generally that was also initiated in March 1999<sup>10</sup> that resulted in suspended decision notice D12/99.

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<sup>4</sup> “Interconnection Rates in the Irish Telecommunications Sector”, November 1998, ODTR 98/52 and “Interconnection Rates in the Irish Telecommunications Sector – Report on Remaining Reference Interconnect Offer Rates”, November 1998, ODTR 98/60

<sup>5</sup> ODTR 99/17 “The Development of Long Run Incremental Costing for Interconnection”, March 1999

<sup>6</sup> ODTR 99/38 containing Decision Notice D6/99 and Report on Consultation Paper ODTR 99/17

<sup>7</sup> ODTR 99/35 “Accounting Separation and Publication of Financial Information for Telecommunications Operators - Decision Notice D5/99, Consultation Report and Issues for Further Consideration

<sup>8</sup> ODTR 99/52 “Accounting Separation and Publication of Financial Information for Telecommunications Operators - Decision Notice D10/99

<sup>9</sup> ODTR 99/43 “Costing Methodologies for use in Accounting Separation - Decision Notice D8/99 and Report on the Consultation”,

<sup>10</sup> Telecom Éireann’s Reference Interconnection Offer, Consultation Paper; ODTR 99/16.