



Commission for
Communications Regulation

Preliminary Consultation - Call For Input

Costing and Financing of Universal Service Obligations

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All responses to this Call for Input should be clearly marked:-
“Reference: Submission re ComReg 10/77” as indicated above,
and sent by post, facsimile, e-mail or on-line at www.comreg.ie
(current consultations), to arrive on or before **Thursday, 21st
October 2010**, to;

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Please note ComReg will publish all inputs, subject to the
provisions of ComReg’s Guidelines on the Treatment of
Confidential Information – ComReg 05/24.

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1 Introduction

This preliminary consultation document is published by the Commission for Communications Regulation (“ComReg”) to seek, through a call for input, the initial views of stakeholders on a range of issues related to the costing and financing of Universal Service Obligations (“USO”).

The European Communities (Electronic Communications Networks and Services) (Universal Service and Users’ Rights) Regulations 2003, (“the Regulations”), provides that the Universal Service Provider (“USP”) may submit a request for funding for the net costs of meeting a USO. ComReg is obliged, under EU and domestic law, to assess any such request.

The universal service in Ireland consists of the provision of a defined minimum set of services to all end-users at an affordable price.¹ Eircom is presently designated as the USP until 30 June 2012². It should be noted that the Regulations allow for the possibility of designating one, or more, undertakings as the USP and that such USP’s may be required to fulfil the USO in one, or more, different geographic areas. ComReg’s Strategy Statement (ComReg 10/47) stated that ComReg would seek to develop its approach to the costing and financing of USO, taking account of the views of all stakeholders. There are a range of issues which must be considered when determining whether, or not, there may be an unfair burden associated with meeting a universal service obligation, including how to evaluate the concept of unfair burden, the costing methodology to be used in determining net costs and how to estimate and treat any intangible benefits.

While it is proposed that a detailed formal consultation will be published in November 2010 on the costing methodology of the USO with respect to requests for funding by a USP for the period 2009/2010, and subsequent periods, it is intended that the consultation process would now commence by seeking views from stakeholders on matters that they consider relevant to such a detailed consultation. The purpose of this document is to provide an opportunity for interested parties to identify any key issues that they believe should be considered by ComReg from the outset. The document sets out certain issues, on an indicative basis, that are likely to be relevant however, at this stage, these are not intended to be in any way definitive. All inputs received to this Call for Input will inform the formal consultation in November 2010 and will not be responded to separately. It is further proposed that a Decision/Information Notice on this subject will be issued by 30 April 2011.

To assist stakeholders prepare their responses to this Call for Input, ComReg has set out below background information relevant to these issues.

Finally, stakeholders should note that, in the event that ComReg determines that there is an unfair burden and net cost of meeting a USO, consideration will also be

¹ See Annex 1.

² ComReg Document No. 10/46.

given to how any sharing mechanism would operate. ComReg is interested, at this time, in eliciting the views of stakeholders on the establishment of a sharing mechanism and how such a sharing mechanism would operate, and ComReg is proposing to issue a formal consultation on the financing of the USO.

Mike Byrne
Commissioner
Commission for Communications Regulation

2 Methodology for Calculation of Net Costs

Regulation 11 of the Regulations makes provision for the costing of universal service obligations³. Regulation 11(4) (2) stipulates that the net cost calculation must be carried out in accordance with Schedule 2, Part A of the Regulations.

Schedule 2, Part A of the Regulations (reflecting Annex IV of the Universal Service Directive) states that the net cost of USO is to be calculated as the difference between the net cost for a designated undertaking of operating with the USO, and operating without the USO. The Schedule further provides that costs arising from uneconomic USO services provided by a USP, as well as groups of end-users that the USP is required to serve on an uneconomic basis, should be included in the net cost calculation. Finally, the calculation should assess the benefits, including intangible benefits, to the operator.

2.1.1 Approach to costing methodology

The selection of a particular costing methodology is left, under the Community legislation, to the Member States and, under the Irish legislation, to ComReg.

The Table below illustrates a number of basic methodologies that could be used for a USO net cost calculation:-

	Top-down		Bottom-up		
	Historic costs	Current costs	Historic costs	Current costs	
FL - LRAIC		?		?	Currently in use in Ireland for LLU prices Commonly called BU LRAIC
FDC	?	?			Commonly called TD LRAIC
	Commonly called HCA	Commonly called CCA			

It is noted that, with respect to the USO net cost calculation, several countries use a Historic Cost methodology (France, Italy), whereas others use a Current Cost methodology (Spain) or a Long Run Average Incremental Costs (“LRAIC”) methodology (United Kingdom). It is also noted that Schedule 2 of the Regulations provides that due attention is to be given to correctly assessing the costs that any designated undertaking would have chosen not to incur, had there been no USO. ComReg has, in the past, indicated a preference for the Historic Cost Accounting (“HCA”) costing methodology however, at this time, ComReg will consider all responses to this Call For Input to inform its approach. (The acronyms referred to in this section can be found in Annex 4).

³ European Communities (Electronic Communications Networks and Services) (Universal Service and Users’ Rights) Regulations 2003.

2.1.2 Approach to cost allocation

According to Schedule 2 of the Regulations, there are two types of specific USO net costs; (1) end-users, or groups of end-users, which would not be served by a commercial operator, and (2) elements of USO services which can only be provided at a loss. The calculation of the net costs of the specific aspects of USO should be made separately to avoid double-counting. The overall net cost of USO is to be calculated as the sum of the net costs arising from the specific components. For this reason, a relevant issue is how cost/revenues vary on an area-by-area basis (or a customer-by-customer basis) to assess USO net costs related to end-users, or groups of end-users, that would not be served by a commercial operator.

It is recognised that there are differing approaches that could be used to distribute the avoidable costs per groups of users, (by Main Distribution Frame⁴ - “MDF”) and per user (per line), with respect to geographical analysis of the cost base, including a Top-Down (TD) approach, a Bottom-Up (BU) approach or in combination:

- A “TD” approach utilises total costs data taken from the accounting system and directly distributes costs per MDF and per line
- A “BU” approach utilises network technical description (number of lines, length of lines, length of trenches, etc) to directly assess costs per MDF and costs per line
- A hybrid approach may utilise a “BU” approach to calculate allocation keys and “TD” approach to apply these keys.

Schedule 2 of the Regulations specifies inter alia that “*Due attention is to be given to correctly assessing the costs that any designated undertaking would have chosen to avoid had there been no universal service obligation*”. Accordingly, an assessment of which costs would be avoided in the absence of a USO may be important. In particular, this may have implications for the allocation of costs, including common costs.

In providing views in relation to USO costing, stakeholders may also wish to advise ComReg of any other methodologies or practical considerations for implementation that, in their opinion, may be appropriate in an assessment of USO net costs.

2.1.3 Efficiency

It is noted that Directive 2002/22/EC requires that the net cost calculation should consider the efficiency of the USP when determining USO net cost;

“National Regulatory Authorities are to consider all means to ensure appropriate incentives for undertakings (designated or not) to provide universal service obligations cost efficiently”

⁴ MDF – also known as a telephone exchange area.

ComReg, at this time, has no preferred methodology for considering the efficiency of the USP and will consider all responses to this Call For Input to assist in informing its approach.

3 Determining if there is an Unfair Burden

The Universal Service Directive⁵ aims to ensure that basic telephone services are available at an affordable price and specified quality, irrespective of geographical location, within Ireland. There are both social and economic grounds for the USO, for example, to provide services to assist vulnerable users and those in remote locations that the market might otherwise not choose to serve, thereby facilitating greater participation by those users in the market. The USO is, therefore, focused on ensuring that everyone, irrespective of location, social standing or income can access basic telecommunications services, thus bringing benefits to those with low incomes who have difficulty in affording a telephone service, consumers with disabilities who need particular services or facilities, and those in rural locations for whom the cost of gaining access to service might otherwise be prohibitive. It is noted that there also exists a positive externality – that is the decision to connect to the PSTN (“public switched telephone network”) confers a benefit on all subscribers to the network and not just the individual who is contemplating becoming a subscriber. Therefore, a communications network is more valuable when increased number of individuals, firms and other organisations are connected to it.

3.1 Evaluating the concept of unfair burden

A decision to establish a sharing mechanism is subject to a finding by ComReg that a USP is, on the basis of a USO net cost calculation, subject to an unfair burden and that there exists a net cost in meeting a USO. Therefore, a determination of what constitutes an unfair burden is fundamental to the process of determining whether, or not, a sharing mechanism should be developed. It is to be noted that a finding of a net cost does not automatically suggest that an unfair burden exists.⁶

Where it is determined that there are USO net costs after intangible benefits have been taken into account, an unfair burden assessment methodology could include an assessment of the effects of a USO on the competitive stance of a USP. The following indicators, amongst others, could be considered:

- USP market share and its evolution
- USP ARPU compared to ARPU of other operator’s
- USP EBITDA margin compared to those of other operator’s, and
- The USP’s ability to recover its costs in aggregate having regard to the strength of competition in relevant markets.

In providing views in relation to the unfair burden concept, stakeholders may wish to suggest alternative, or additional, objective criteria which may be used when

⁵ Directive 2002/22/EC

⁶ CoCom 06-21, Brussels, 14 June 2006

assessing the burden of USO, if any. ComReg would also value inputs relating to the indicators set out above.

3.2 Methodology for determining intangible benefits

In addition to potential costs incurred in meeting a USO, USP's may also benefit in certain ways from universal service provision. These benefits represent the positive effects on the USP of providing a universal service which have not been accounted for in the costing methodology. Once the value of these benefits has been determined, it is deducted from the cost of the USO.

In accordance with Schedule 2, Part A of the USO regulations, the net cost calculation must take into account the market benefits, including intangible benefits, to the USP. The intangible benefits that may arise for a USP include;

- Brand Recognition
- Ubiquity
- Customer Life Cycle
- Potential future sales of services
- Goodwill
- Marketing
- Payphone Advertising

It is noted that the benefits outlined above vary in significance and that the values which have been calculated for these benefits vary across countries. In the EU, in countries where USO costs have been calculated, brand recognition is often recognised as the most significant benefit. For example, in 2003/04, Ofcom⁷ estimated total benefits of €70-€76m arising from the USP designation, of which brand enhancement was valued at €60-€62m; and, in 2007, CMT⁸ valued total benefits at €16.27m, €9m of which arose due to brand enhancement.

ComReg recognises that defining, and estimating, the benefits of being a universal service provider may be approached in various ways, through a range of alternative methodologies. ComReg, at this time, has no preferred methodology for defining, and estimating, the intangible benefits and will consider all responses to this Call For Input to assist in informing its approach.

⁷ Ofcom - Review of the Universal Service Obligation, 14th March 2006.

⁸ <http://www.cullen-international.com/report/3049/c35527>

4 Financing of USO

Where it is determined that the net cost of meeting a USO may represent an unfair burden on the USP, ComReg is obliged to establish a sharing mechanism (“universal service fund”) to apportion the net cost. Regulation 12 of the Regulations makes provision for the financing of universal service obligations, as follows:

“Where the Regulator, on the basis of the net cost calculation referred to in Regulation 11, finds that the net cost of meeting an obligation under Regulation 3, 4, 5, 6, 8 or 9 represents an unfair burden on an undertaking it shall apportion the net cost of the universal service obligation among providers of electronic communications network and services.”

ComReg is interested, at this time, in eliciting the views of stakeholders on the establishment of a sharing mechanism and how such a sharing mechanism would operate, if an unfair burden and net cost of meeting an obligation was determined. As stated earlier, ComReg is proposing to issue a formal consultation on the financing of the USO.

ComReg notes that there are a variety of methodologies used in countries where a sharing mechanism has been established to apportion the net cost. For example, in France, public network operators and providers of electronic communications services make a contribution in proportion to their turnover (less interconnection revenues) and, as a result, operators with a turnover below €5m are exempt from making a contribution. In Austria, large operators voluntarily agreed to share the net costs.

The Regulations set out the principles to which any sharing mechanism should adhere and, in addition, permit the Regulator to exempt some undertakings from contributing to any sharing mechanism. ComReg will, therefore, consider which operators, if any, should be required to make contributions, should an unfair burden and net cost of meeting an obligation be determined. ComReg will also consider whether there should be a threshold below which operators, if any, would be exempt from making a contribution and, if so, how this threshold should be determined. In addition, ComReg will consider whether such an exemption would be considered in the context of, for example, audited turnover, and the services to be included when calculating such indicators.

5 Submitting inputs and views

The Commission welcomes all written responses from stakeholders by 21st October 2010. ComReg will, in the interest of openness and transparency, publish all non-confidential inputs received and would, therefore, request that electronic submissions be submitted in an unprotected format so that they can be published electronically. Submissions will be published subject to the provisions of ComReg's Guidelines on the Treatment of Confidential Information - ComReg 05/24. Any confidential material should be clearly identified and placed in a separate Annex to the response.

Annex 1 - Scope of USO

ComReg’s approach to universal service scope and designation is in accordance with the European Communities (Electronic Communications Networks and Services) (Universal Service and Users Rights) Regulations 2003 (“the Regulations”). The Regulations transpose the Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on universal service and users’ rights relating to electronic communications networks and services (Universal Service Directive) (“the Universal Service Directive”) into Irish law.

ComReg notes that Directive 2002/22/EC of the European Parliament was amended by Directive 2009/136/EC (“Amending Directive”) and notified in the Official Journal on 18 December 2009.¹ The Amending Directive must be transposed into Irish law by 24 May 2011. Furthermore, on 3 March 2010, the European Commission issued a public consultation (consultation on future universal service in digital era)² which may result in changes in the scope of universal service; however the impact, or timing, of any changes arising from this review is not yet clear.

As the designated USP, eircom must comply with the following obligations.

Provision of access at a fixed location

The USP must satisfy any reasonable request to provide connections to the public telephone network and access to publicly available telephone services. Any connection provided by the USP must be capable of:

1. Local, national and international telephone calls
2. Facsimile (fax) communications
3. Data communications at data rates that are sufficient to permit functional internet access (the USP is currently required to adopt 28.8kbps as a reasonable minimum data rate).

The USP is required to consider all requests for connections as reasonable if the expenditure involved in meeting the request is less than €7000 and the cost to the applicant shall not exceed the standard connection charge.

Requests for connections which involve expenditure in excess of €7000 are to be considered reasonable if the applicant agrees to pay the standard connection charge plus incremental costs above €7000.

Directory Services and Directories

The USP is required to provide end-users a comprehensive printed directory of subscribers, free-of-charge and updated at least once a year. In addition, the USP must keep a record in the NDD of all subscribers of publicly available telephone services in the State, including those with fixed, personal and mobile numbers who have not refused to be included in that record and allow access to any information contained in such a record to any such other undertaking, or any person, in accordance with the terms and conditions approved by ComReg.

Public pay telephones

The USP shall ensure that public pay telephones are provided to meet the reasonable needs of end-users in terms of geographical coverage, number of telephones, accessibility of such telephones to users with disabilities and the quality of services. Payphones that are covered under the USP are those available on the street and in other public areas available to the public at all times (i.e. unrestricted access).

Specific measures for users with disabilities

The USP must provide a dedicated section of its website, accessible from the homepage, with information on the services that it provides which are of particular interest to people disabilities.

The USP shall maintain a Code of Practice concerning the provision of services for people with disabilities and shall periodically review and, where appropriate, amend the Code in consultation with the National Disability Authority (NDA) and other representative bodies.

The USP must provide the specific services for users that are hearing impaired; users that are hearing and/or speech impaired; users with limited dexterity or mobility; users with restricted vision and users unable to use the phone book due to a disability.

Affordability

The Regulations require that the USP adheres to the principle of maintaining affordability for universal services. Currently, affordability is maintained through a number of measures, including:

- Within the price cap regime, an overall safeguard control on consumers bills (online rental and calls)
- The Department for Social Protection's Free Telephone Rental Allowance (FTRA) under the Household Benefit Scheme
- Eircom's low usage scheme - the Vulnerable Users Scheme

Annex 2 – Regulation 11 of the European Communities (Electronic Communications Networks and Services) (Universal Service and Users’ Rights) Regulations 2003

- (1) Where an undertaking designated as having an obligation under Regulation 3, 4, 5, 6, 8 or 9 seeks to receive funding for the net costs of meeting the obligation concerned, it may submit to the Regulator a written request for such funding.
- (2) A request under paragraph (1) shall be accompanied by such supporting information as may be reasonably required by the Regulator for the purposes of paragraph (3). The data may be based on such period as may be specified by the Regulator.
- (3) The Regulator shall, on the basis of such information, including information supplied pursuant to paragraph (2), as it considers sufficient to enable a determination under this paragraph to be made, determine whether an obligation referred to in paragraph (1) may represent an unfair burden on the undertaking concerned.
- (4) Where the Regulator determines that an obligation referred to in paragraph (1) may represent an unfair burden it shall calculate the net costs of its provision, based on-
 - (a) the net costs, taking into account any market benefit which accrues to the undertaking, calculated in accordance with Schedule 2, Part A, or
 - (b) where applicable, the net costs identified by a designation method in accordance with Regulation 7(3).
- (5) A designated undertaking referred to in paragraph (1) shall provide such information as is reasonably required by the Regulator for the purposes of paragraph (4).
- (6) Where the Regulator determines that an obligation referred to in paragraph (1) may not represent an unfair burden it shall notify the undertaking concerned of that determination, together with the reasons for the determination as soon as reasonably practicable after the determination is made.
- (7) The accuracy of the accounts or other information or both, serving as the basis for the calculation of the net cost of an obligation shall be audited or verified, as appropriate, by the Regulator or by a body independent of the undertaking concerned and approved of by the Regulator.
- (8) The Regulator shall make publicly available the results of the cost calculations and the conclusions of any audit or verification undertaken pursuant to this Regulation.

Annex 3 – Regulation 12 of the European Communities (Electronic Communications Networks and Services) (Universal Service and Users’ Rights) Regulations 2003

- (1) Where the Regulator, on the basis of the net cost calculation referred to in Regulation 11, finds that the net cost of meeting an obligation under Regulation 3, 4, 5, 6, 8 or 9 represents an unfair burden on an undertaking it shall apportion the net cost of the universal service obligation among providers of electronic communications network and services.
- (2) The Regulator shall establish a sharing mechanism administered by it or by a body independent from the designated undertakings, which body shall be under the supervision of the Regulator. Only the net cost, as determined in accordance with Regulation 11, of the obligations provided for in Regulation 3, 4, 5, 6, 8 or 9 may be financed.
- (3) A sharing mechanism established under paragraph (2) shall respect the principles of transparency, least market distortion, non-discrimination and proportionality in accordance with the principles of Schedule 2, Part B. The Regulator may choose not to require contributions from undertakings whose audited national turnover is less than such amount as may, from time to time, be specified by the Regulator, having regard to any views expressed to it pursuant to any consultations carried out in accordance with Regulation 27.
- (4) Any charges related to the sharing of the cost of universal service in accordance with an apportionment under paragraph (1) shall be unbundled and identified separately for each undertaking.
- (5) The Regulator shall not impose any charges pursuant to this Regulation on undertakings that are not providing services within the territory of the State.
- (6) The Regulator shall notify each undertaking required to share the cost of a universal service obligation of its obligation to contribute to such cost including the amount, manner and timing of payments to be made.
- (7) An undertaking which has been notified of its obligation to contribute an amount specified by the Regulator shall pay that amount in the time and manner specified by the Regulator.
- (8) Any amount payable to the Regulator under this Regulation that remains unpaid may be recovered by the Regulator as a simple contract debt in any court of competent jurisdiction and any such amount shall include interest at the rate per annum standing specified for the time being in section 26 of the Debtors (Ireland)

Act 1840, on the amount or part thereof remaining unpaid in respect of the period between the date when such amount or part thereof fell due and the date of payment of such amount or part.

(9) The Regulator shall, subject to the protection of the confidentiality of any information which it considers confidential, publish an annual report setting out the calculated net cost of universal service obligations, identify the contributions made by all the undertakings involved and identifying any market benefits that may have accrued to any undertakings designated by the Regulator under Regulation 7.

(10) The Regulator shall, subject to the Freedom of Information Acts 1997 and 2003, maintain and accept as confidential any information provided under these Regulations by an undertaking providing electronic communications networks or services expressed by it to be confidential, except where the Regulator has good reason to consider otherwise.

(11) The Regulator shall publish and make publicly available all information in relation to the principles used for cost sharing, including the details of the mechanism used.

Annex 4 – Costing methodologies - Acronyms

FL-LRAIC	Forward Looking - Long Run Average Incremental Costs
FDC	Fully Distributed Costs
CCA	Current Cost Accounting
HCA	Historic Cost Accounting
BU- LRAIC	Bottom Up - Long Run Average Incremental Costs
TD- LRAIC	Top-Down - Long Run Average Incremental Costs