

## Appendix II



POST AND TELECOM  
ADMINISTRATION  
IN ICELAND

**Conclusions on PTA consultation on the Draft PTA  
Decision regarding cost analysis by Siminn hf. of  
wholesale prices for access to the public telephone  
network at a fixed location for residential and non-  
residential customers**

**April 2015**

## TABLE OF CONTENTS

	<b>Page</b>
1 Introduction.....	3
2 Risk-free interest.....	4
3 Efficiency and automation .....	5
4 Discount terms .....	6
5 Reference offer on resale and access to the Siminn fixed line network .....	7

# 1 Introduction

This document contains an overview of the replies and comments received in the Post and Telecom Administration (PTA) consultation on the Draft Decision with respect to cost analysis of wholesale access for access to the public telephone network at a fixed location for residential non-residential customers (market 1). The initial draft was presented to stakeholders for consultation on the Administration's website on 22 December 2014 and the consultation was concluded last 13 February.

The following parties submitted comments on the Preliminary Draft.

- Hringiðan ehf. (Hringiðan)
- Símafélagið ehf. (Símafélagið).

Símafélagið objections were sent for comment to Siminn and Siminn's responses are specified here below, following individual comments made by Símafélagið.

Comments are categorised by subject. Endeavours have been made to identify all significant comments and to answer them. At the end of each comment there is a short summary of the position of the PTA.

## 2 Risk-free interest

**Hringiðan** objected to the fact that the PTA used the rate of return in HFF 150644 as a basis for the calculation of weighted capital costs for Siminn hf.

Hringiðan considers it very contentious for housing bonds from the Housing Financing Fund to be considered risk-free interest and indicates news coverage of matters related to the Housing Financing Fund during recent years. It would be much more appropriate to use state bonds as a reference, as is customary, and that RIKS 21 0414 was the only indexed state bond registered on the market today. The average rate of return on this bond from 1 April 2010 to 31 December 2013 was 2.51% against the 3.26% which is used as a reference in the Siminn cost analysis.

Hringiðan pointed out that such a difference had a significant impact on the cost analysis and that it increased all prices correspondingly.

Hringiðan requested that the PTA use state bonds as a risk-free interest base in the calculations and not housing bonds from the Housing Financing Fund.

### **The position of the PTA**

As stated in Section 3.2.1 in the consultation document, the risk-free interest used as a reference in the pricing is 3.13% for the operational year 2013 and this is used as a basis for the cost analysis and not 3.26% as maintained by Hringiðan.

The PTA uses interest on indexed state bonds or on bonds with state guarantee with a duration of 10 years or longer for the purpose of calculating risk-free interest. The PTA considers that the ten-year duration or longer reflects the lifetime of the assets in question.

The PTA uses five-year average interest (2009-2013) while the RIKS 21 0414 category is not calculated longer than 3.75 years at this time which means that the comparison period is not the same as the one used by Hringiðan. The PTA considers it proper to use average interest for the preceding 5 years, as the methodology is intended to prevent temporary fluctuations in interest having an abnormal impact on the rate of return and thus on the pricing of the service in question. This is a case of implementation over a period of many years, which has not been disputed up to this point in time.

In order to estimate risk-free interest, the PTA has up to this point in time used HFF 1504 2034 30 year indexed Housing Financing Fund bonds and not HFF 1506 2044 as stated by Hringiðan.

It is however correct that in very recent years the development on the market has been that Housing Financing Fund bonds no longer reflect risk-free interest, as a special risk premium has formed on Housing Financing Fund bonds because of uncertainty about the future of the Fund. The above does not however have a significant impact on the PTA calculations of risk-free interest today (impact on average interests with reference to the five-year period 2010-2014), as from and including the operational year 2014, the PTA uses figures that are adjusted for the risk premium. The PTA plans to examine whether there is reason to change its reference with respect to the bond category. If this examination were to lead to changes to the reference

with respect to bond category, then this would not come into force until the next cost analysis which would be based on the cost base for the year 2014 or 2015 and would therefore have no impact on the cost analysis here under discussion.

### **3 Efficiency and automation**

With respect to increases in prices for access, **Símafélagið** pointed out that there was every likelihood that increased efficiency had been achieved in recent years by decommissioning telephone exchange equipment in many telephone exchanges across the country in favour of central equipment. Increased efficiency resulting from less equipment and fewer operations locations should thus have reduced costs and not increase them.

#### **Siminn reply**

Siminn pointed out that the company had decommissioned nine remote subscriber switches and one telephone exchange (Miðbær) and that this was taken fully into account in the cost analysis. Siminn uses replacement cost in its calculations and takes into account investments in recent equipment.

#### **The position of the PTA**

The PTA refers to the Siminn reply and sees no reason to make further comments on this issue

**Símafélagið** points out that in connection with other service items, Siminn has introduced increased automation in processing of requests. In the year 2011 the time used by Siminn technicians to process requests had been specified and that given these changes one could assume that time required for technicians would be insignificant today. In addition to this one could assume that experience and operational procedures had developed significantly during this period which should lead to even further efficiency.

#### **Siminn reply**

Siminn pointed out that the introduction of automatic processes was still ongoing and for this reason the impact that such automation would have on the pricing of these aspects was unclear. It should be noted that the automation now in process only covers local loops with PSTN service. Today there is significant work being done on implementation of these processes and this work will continue. In addition to this one can point out that the introduction of automatic processes results in other costs, in investments in equipment, programming, operations, processes and monitoring. The main objective of automation is to endeavour to ensure accuracy of information between electronic communications companies and to make such processes more automatic.

#### **The position of the PTA**

The PTA agrees with Símafélagið that one should take automation into account and the economies that it brings. On the other hand, this information is not currently available and for this reason the PTA proposes that Siminn make a special examination of those service items that are based on time measurement in the next review of this cost analysis.

## 4 Discount terms

**Símafélagið** requested that it be examined whether a discount according to the number of connections harmonised with competition considerations and pointed out that in the Skipti Settlement with respect to Mila there was no incrementally increasing discount for those services not covered by the Settlement. Such a system of discounts could create discrimination between larger and smaller electronic communications companies and could increase access barriers to the market.

### **Siminn reply**

Siminn replied that the company's discount terms took into account the economies inherent in selling many local loops to the same party. Discount is only given on the Siminn mark-up on the local loop charge from Mila and Siminn refers to its exchange of letters with the PTA from September 2013. The current arrangement for discount terms is agreed in the PTA Decision no. 8/2013 and is based on objective discount criteria. Siminn points out that Símafélagið made no objections when the terms in question were being discussed. Siminn refers in this connection to the PTA Decision no. 24/2013 and to the PTA discussion on the discount.

In the opinion of Siminn, the PTA has assessed and taken a position on these objections. There is basically no change being made to the discounts, only the pricing is being changed. Then Siminn also points out that in the Competition Authority Decision no. 6/2013 there was no discussion on the pricing as such.

### **The position of the PTA**

The PTA refers in its discussion on this aspect in its Decision no. 24/2013:

*"The PTA considers there to be no doubt that an increased number of connections brings increased efficiency with respect to total handling of access to the Siminn telephone exchanges as the cost of handling access to the system is to a large extent fixed cost. The PTA emphasises that a discount on handling costs is in effect the provision of a discount on the basis of evaluation of increased efficiency resulting from an increased number of connections and it is not a case of giving a discount on the cost price of telephone exchanges or local loops.*

*The PTA considers the Siminn cost assessment for handling of the access in question to be logical, given the cost of providing and general handling of access to the company's systems and in addition to this the Siminn reference to the number of connections is reasonable compared with the total number of connections in the Siminn system. For this reason the PTA accepts the Siminn proposal with respect to the revised table on quantity discount for connections."*

As is stated in the PTA Decision, the Administration plans to prescribe that in the next cost analysis a cost assessment shall be for time measurements etc. and that this assessment should be used as a basis for calculating the tariff rather than a fixed percentage mark-up on Mila local loops. The above may have an impact on the existing discount arrangement.

## 5 Reference offer on resale and access to the Siminn fixed line network

**Símafélagið** points out that Siminn has two kinds of wholesale of telephone service, on the one hand pre-selection where traffic is directed to the purchaser who is responsible for routing and invoicing, and on the other hand resale, so called "Reference offer for resale access to the Siminn fixed line network" where Siminn is responsible for all functions. It was extremely important that all price changes applied to both agreements (and were applied at the same time) so that the situation did not arise where the price for a less service was higher than for more service. Such inconsistency would make it impossible for those who offer such service in resale to compete with Siminn. In reality the price for full service should be higher than for pre-selection. Today these prices were on the other hand the same, even though significantly more service was provided in resale agreements, see items 2.2 and 2.3 in Appendix I on page 19 in the Siminn resale agreement.

### **Siminn reply**

Siminn points out that resale parties pay a higher rate than parties in SB-CPS service in the form of an annual access charge. One must keep in mind that the tariff for traffic charges are the same for resale as for SB-CPS as they constitute comparable use of system units in the Siminn fixed line telephone system. As the charges are effectively the same the price changes take place at the same time regardless of whether the service is resale or SB-CPS

### **The position of the PTA**

The PTA agrees with Símafélagið that it is necessary for these price changes to apply to both agreements and to take place at the same time, and it is stated in the PTA Decision no. 36/2012 that Siminn shall publish an analogous reference offer on resale and access. This is also in accordance with statements made in Siminn replies and the company intends to alter prices for comparable service in resale access at the same time.