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AIIP Comments on

ERG Public Consultation on a draft Common Position on Symmetry of Mobile/Fixed call Termination Rates

Introduction

The assumptions underlying ERG consultation are clear: "... *symmetry can concern either remedies (symmetry in remedies meaning the same remedy for fixed or mobile operators) or termination rates (symmetry in rates meaning there exist a single termination rates for all fixed or all mobile operators).* ***The present document mainly focuses on the second type of symmetry, i.e. termination rates symmetry and investigates the conditions under which it could be advisable for NRAs to impose symmetric termination rates to notified operators***" (ERG document, page 5).

Since the second type of symmetry (i..e convergence on a single TR applied by all operators) presupposes that is already achieved by the different NRAs (in each EU Country) an harmonized approach on the application on the symmetry in remedies (first type of symmetry, i.e. same approach towards cost orientation), while the experience shows quite the contrary.

As a matter of fact, as acknowledged by ERG itself, "*NRAs may have imposed to SMP operators different price control remedies or have specified the same remedy differently, especially using different cost analysis tools and methodologies leading to heterogeneous cost references. Consequently, the absolute level of termination rates currently enforced and the resulting asymmetries are quite different across Europe, even though over time a narrowing of the differences in the methodologies used and accordingly in the asymmetries can be observed*" (ERG doc., pag. 5). Therefore, there is still much harmonization activity as to cost orientation principles and accounting methods and tools to be carried out before even thinking of symmetry in TR[1].

Therefore, any intervention aimed at suddenly imposing symmetric TR obligations, without a prior harmonization in cost accounting remedies and principle as well as in cost analysis tools and methodologies would be disruptive for European operators activities in 18 out of 26 Countries[2].

Instead, by setting cost oriented termination rates NRAs should avoid excessive pricing and productive inefficiency but, at the same time, should ensure sustainable competition and avoid distortion of competition in retail downstream markets, by preventing SMP operators (in the upstream markets) from Raising Rival Cost, price squeeze practices and cross subsidisation.

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[1] Such a need is also confirmed by ERG statement that "*Regarding mobile termination rates, this work will be followed up with a new project team focusing on the harmonisation of methods used by national regulatory authorities to implement the cost orientation remedy*" (ERG Consultation document, pag. 1). AIP suggest that this project team should act ASAP and in any case before any further amendment in regulation tools.

[2] Consultation document, page 26.

In addition, as we shall in more details later (under G.1), the consultation moves from a second wrong assumption.

As a matter of fact the statement that symmetry in TR is the best way to grant competition and efficiency on the market is correct if and only if (since it assumes that) market structure is featured by no entry barriers and competitors having similar sizes[3], scale economies and (therefore) cost structures. The Commission is therefore assuming that the market is featured by the (theoretical) perfect competition conditions.

However, the electronic communications markets have always been featured by the following –non transitory- features which, without regulation, would bring to the "natural monopoly":

- huge sunk costs;
- information asymmetries;
- increasing scale (and scope) economies, which would lead to descending unit cost for increasing total production output[4];
- strong network effects which, absent certain regulatory obligations aimed at achieving a unitary virtuous effect and to create a Open Network (such as interoperability), becomes detrimental externalities for smaller competitors;
- scarcity of resources, as to spectrum frequencies.

Under a dynamic analysis of the market one should also consider that the effects of such features are enhanced and even stronger in a converging environment, where the sum of all of them, each of which would affect any of the converging layers (fixed infrastructure, mobile infrastructure, encoding/decoding software, DRM, etc.), has an exponential concentrative effect.

It is therefore fallacious ERG statement that "*in this context it may be difficult to justify a decision not to provide the same incentives to all operators and it may not be clear why OAOs should not be as efficient as incumbents*" (p. 36) since the market itself is featured by the above mentioned non transitory elements which justify a different level of efficiency between incumbent and OAOs, which may not be reversed nor overcome, unless with asymmetric measures of regulation.

AIIP believes that symmetric FTR and MTR (with TR converging for all operators on the one determined for incumbents) would actually be in prejudice of a fair and sustainable competition in the retail downstream markets, discriminate amongst operators and result in a new legal barrier to access markets for the provision of fixed, mobile and convergent services, to the detriment in the

[3] Which is not the case, as evidenced by the circumstance that "*Data on the percentage of subscribers in direct access have been grouped into five classes, ranging from countries where such percentage is below 5 to countries where it is above 20. Table 3 shows that for 8 countries, the percentage of subscribers in direct access is very low (≤ 5). In 7 countries, the percentage of subscribers in direct access is between 5 and 10, while it is equal or greater than 20 in 4 cases*". (ERG, pag. 16). Moreover, as evidenced by figg. 3-4, incumbent market shares in 19 out of 22 Countries exceed 85%, and in the last three range from 71,2% to 78,2% (ERG, 19-20).

[4] From data under footnote 3, ERG derives that "*…the level of markets shares on access markets is often used as an indicator of the economies of scale realizable by operators. Data shown in the above figures should lead to conclude that only incumbent operators are able to realize considerable economies of scale*" (ERG, 21).

long run of end-users. Therefore, by imposing a unique symmetric TR, NRAs would not only fail in promoting competition but also distort competition itself.

ERG should therefore encourage NRAs to worry more about the quick path of incumbents' TR towards effectively cost oriented TR, rather then seek a glide path towards a unique and symmetric TR for all operators, which would (at least in Italy) jeopardize fair and sustainable competition in the retail downstream markets.

It seems that ERG is attempting to give an *ex post* rationale to an amendment to regulation already anticipated by the Commission which "*In the frame of Article 7 procedures .... increasingly invites NRAs to make termination rates asymmetry disappear*" (ERG doc., pag. 5).

According to AIIP such a "*learning by doing approach*" in regulation may lead to serious and unrecoverable damages to market structure.

Therefore, AIIP invites ERG and the Commission to strongly concentrate on achieving in the short term the above harmonization in cost accounting remedies and principle as well as in cost analysis tools and methodologies before taking any further regulatory step.

PART 1: GENERAL ECONOMIC PRINCIPLES OF TERMINATION RATES REGULATION

QUESTION G1: DO YOU THINK THAT THE PRINCIPLES OUTLINED IN THE GENERAL ECONOMIC INTRODUCTION COVER ADEQUATELY THE UNDERLYING ECONOMIC SITUATION OF BOTH MOBILE AND FIXED TERMINATION MARKETS? IF YES, DO YOU THINK THEY ARE SUFFICIENTLY REFLECTED IN THE TWO PARTS ON "MTR SYMMETRY" AND "FTR SYMMETRY" AND THAT THEY ARE CONSISTENTLY APPLYING THE PRINCIPLES? IF NO, WHAT DO YOU THINK IS MISSING AND WHICH REASONING SHOULD BE ADDED?

According to ERG "*economic principles tend to recommend the setting up of a unique and uniform termination rate for all network operators ... raising thus numerous regulatory questions NRAs have to face and to answer* ...[such as] *what is the most appropriate method for the enforcement of TR symmetry? ...could objective cost differences justify asymmetry?... How could perverse effects of TR symmetry (e.g. when traffic is unbalanced) on competition dynamics be avoided* " (page 6).

According to AIIP there are serious deficiencies in the analyses and principles outlined in the general economic introduction. As clarified in the introduction, the ERG draft Common Position subject to Public Consultation appear to be based on wrong assumptions which seem to lead ERG to wrong conclusions.

In addition to the above, AIIP challenges the correctness of all the three main reasons on which ERG based its request to achieve prompt symmetry in FTR. As a matter of fact ERG hold that:

(i) almost ten years have expired since liberalisation took place in EU Countries ad therefore, that enough time has expired for OAOs to recover their costs through different TR (ERG doc., pages 36-37).

However ERG underestimated the circumstance that in certain Countries, such as Italy, the liberalisation only formally took place in 1998, due to abusive behaviours of the incumbent which, among other, exploited their monopsony power in negotiating FTR with OAOs to fix very low termination rates that squeezed their competitors revenues and did not allow OAOs to recover their costs (see Italian Antitrust Authority decision n. 8481, case A-280 *Tiscali-Albacom/Telecom Italia*, in Boll. 28/2000, www.agcm.it).

Therefore, in spite of ERG allegations, in many Countries asymmetry principle was affirmed only recently, such as in Italy where it was applied only after incumbent condemnation by the antitrust authority and a formal statement by the Communications Authority on AOAs right to asymmetric FTR in negotiating with incumbent, which in Italy was made by AGCOM Decision 11/03/CONS, effective since the second half of 2003.

(ii) ERG states that "*it is unclear whether and, if so, to what extent OAOs would suffer from diseconomies of scale relative to the incumbent. Unlike in the mobile sector where generally all operators are subject to coverage obligations … fixed OAOs are free to enter in selected areas – i.e. the ones that are potentially the most profitable – …. In this regard, a fixed OAO operating an a regional basis, using a new technology and an optimized network will presumably be able to reach an efficient scale in a relatively short timeframe. Therefore, the claim that OAOs suffer from dis-economies of scale may not be as strong as sometimes thought. …*" (ERG doc., page 37).

However ERG should base its assumption on real cost calculation and omits to consider that:

(a) although incumbent and OAOs active on the same metropolitan areas have the same installation and realization costs for Metropolitan Area Network, incumbent have a much larger number of clients on which to spread such costs and have a much lower average cost per subscriber; moreover

(b) while mobile networks are featured by rapidly decreasing incremental costs, fixed networks face decreasing incremental cost only if clients are highly concentrated in a given area and, in any case, increasing incremental cost where the cover neighbouring areas.

In this regard, it is noteworthy that according to article 13, on "*Price control and cost accounting obligations*", of the Access Directive (Directive 2002/19/EC), when NRAs impose price controls obligations "*shall take into account the investment made by the operator and allow him a reasonable rate of return on adequate capital employed, taking into account the risks involved*". Therefore, any regulatory decision on price control and cost accounting obligations should balance the need to "*promote efficiency*" with the need to guarantee a "*sustainable competition*".

According to AIIP, any symmetry in FTR should be achieved only after a certain deadline from an operator entry and cannot be set as a general rule, irrespective from the date of entrance on the market by each operator.

As matter of fact, fixing of symmetry in FTR alone, without any tempering of the principles (e.g. for new entrants) would create an entry barrier for new entrants in the communications market and would close the market to new entries (irrespective whether efficient or not).

ERG focuses on symmetric termination rates. Instead, AIIP believes that symmetry in rates is a secondary issue: how to determine cost oriented termination rates is the main issue, and the first goal to be achieved by TR regulation.

Moreover, in relation to point (ii) above, AIIP has serious concerns that there could actually be a unique cost oriented FTR and a unique cost oriented MTR for all operators.

According to par. 3 of art. 13 Access Directive (above mentioned) "*For the purpose of calculating the cost of efficient provision of services, national regulatory authorities may use cost accounting methods independent of those used by the undertaking*", thus NRAs may impose to each firm TR not depending from costs effectively incurred in by operators if necessary to avoid that the latter transfer on final client price their inefficiency. However, this does not mean that NRAs may impose TR which preclude new entrants and small operators to recover their investments (allowing some operators to fully recover costs and denying this possibility to others).

Symmetric regulation should always be intended as the application of the same remedy in the same circumstances, in a non discriminatory manner.

With regard to price control measures, symmetric regulation means the application of the same price setting methodology and costing methods. Symmetric regulation can not mean a single symmetric termination rate for all operators if such a unique rate unduly discriminates new entrants and small operators. Such a regulatory policy would be anticompetitive.

In conclusion, on this regard, AIIP outlines that:

- productive efficiency (which is achieved when firms minimize total cost with respect to technology of production) may differs among operators;
- consequently also the "efficient" termination rate may differs among operators;
- a higher termination unit cost would not imply that such an operator is productively inefficient, or relatively inefficient;
- it is not true that there is a direct relationship between the level of TR and productive efficiency, given that productive efficiency is achieved when firms minimize total cost; as a matter of fact (and as it is also clear from figure 17, page 79, of the consultation document) an operator with higher termination unit costs can be more (relatively) efficient than an operator with lower unit costs; higher termination unit cost may arise from less economies of scale even if the operator minimizes its own total costs (productive efficiency);
- determine a unique termination rate could mean imposing loses to actual and/or potential new entrants and small operators;

- incumbents' current termination rates should represent (according to cost orientation obligation) the cost of an operator with large penetration rates and high market shares and call volumes, which has completed the network roll-out. Assuming this level of termination rates for new entrants not only be discriminatory but would also represent a disincentive for network deployment and expansion by OAOs;
- TR should always guarantee an adequate return to give rise to the following "virtuous cycle": reasonable return of invested capital and adequate margins → development along the ladder of investments → scale economies → lower unit costs → lower cost oriented TR → possible decrease of retail prices in downstream markets;
- the economic theory referred by ERG seems to simply ignore (and/or abstract from) electronic communication market features: huge sunk costs; information asymmetries; increasing scale (and scope) economies, strong network effects, scarcity of resources as to spectrum frequencies, etc. Consequently such economic theory omits to properly assess (a) the effect of SMP on competition (b) effects of remedies proposed;
- ERG conclusions seems to be based on static market analysis which fails in taking in to the right consideration competitive issues related to downstream markets, included issues related with the history of regulation and incumbents' anticompetitive behaviours (see hereinafter for the Italian experience);
- fixing symmetry in FTR as a general rule, without any exception, also for new entrants (irrespective from their date of entry on the market and although limited in the medium term – i.e., 5 to 10 years, which is the term for recovering the investments in the sector), would create an entry barrier.

QUESTION G2: ANY FURTHER COMMENTS REGARDING CONSISTENT REGULATION OF BOTH MTR AND FTR WITH REGARD TO SYMMETRY IS WELCOME.

Consistent regulation of both MTR and FTR should accurately consider the problem of network externalities.

On-net/off-net retail tariffs differentiations is the incumbent's attempt to counter the benefits of larger networks from exploiting network externalities: as incumbents' have the biggest market share their customers tend to make fewer off-net calls. This network effect may be artificially reinforced and become an externality through systematic "on-net" offers (i.e. on-.net calls less expensive than calls to other network).

On the one hand, the possibility for the incumbent to apply on-net prices to its final customers at levels lower than those of wholesale termination charges applied to its competitors implies a general competitive disadvantage for new entrants and operators with smaller market shares: such on-net offers would not be replicable by new entrants and operators with smaller market shares, because their customers would gain less from on-net offers limited to a smaller number of subscribers, and competition harm to the detriment of consumers benefit[5], and suggest the need for asymmetric measures (in this regard, it should be highlighted a mistake in ERG research. According to Table 14 only Estonia would regulate a prohibition on incumbent as to on-net off-net discrimination; however, also in Italy a similar prohibition is set forth by AGCOM Decision no. 642/06/CONS

[5] See ERG consultation paper, pp. 84 ss.

which has been unsuccessfully challenged by the incumbent and has been confirmed by Italian Administrative Courts).

As a matter of fact, the application by the operator with the larger customer basis of prices for on-net communications lower than interconnection fees on their networks applied to third parties forecloses the market to operators with smaller customer basis since the latter cannot match the former prices (unless at the cost of noticeable losses)[6].

On the other hand, the potential downsides to be considered, in a trade-off regulatory decision for asymmetric measures, would be higher termination rates charged by smaller operators and/or new entrants. However their impact on consumers would not depend on the nominal value of terminating rates charged by small operators and new entrants, but on their overall amount. Therefore, in highly concentrated markets or, in any case, when the incumbent still own a large part of the market, the potential downsides would have a limited impact on end users.

As a result, asymmetric regulatory measures in favour of smaller operators and new entrants would probably improve competitive conditions on retail markets by softening the potential adverse effects of the problem identified above: network externalities.

Consistent regulation of both MTR and FTR should also examine the existing relationship between fixed and mobile TR and (therefore) provision of services.

ERG consultation document undervalue the following issue: Fixed-Mobile traffic substitution through on-net policies, and Fixed-Mobile convergence.

As a matter of fact, on-net/off-net retail tariffs differentiations by mobile operators (could) also result in **Fixed-Mobile traffic substitution phenomena** (since "*mobile terminating tariffs are in general more than 10 times as high as fixed terminating*") and in a reduction of fixed network accesses, thus generating network diseconomies, which reduce revenues for fixed network operators and cash flow for financing network investments also to reduce digital divide in the broadband[7].

As recognised also by ERG such a gap between FTR and MTR is not entirely justified by cost differences. Hence ERG should stress to NRAs attention the risks the competitive distortion between Fixed and Mobile operators in favour of the latter which could result from.

AIIP outlines that NRAs should take into account the history of competition and TR regulation in the single national market.

On this regard, AIIP outlines the findings of the Italian Competition Authority (see Decision no. 17131, A357 - *Tele2/Tim-Vodafone-Wind,* of August 3, 2007) on MTR (see hereinafter M1).

[6] As a matter of fact, the value of a good/service within a network (as those at issue) increases remarkably for each user with the increase of the number of users within the network. If the marginal gain of each user for being able to communicate with another user is "1", the total marginal gain of the "n" users belonging to a certain network, that derives from linking one more user to that network is not "*n*1*" buth "*n*(n-1)*".
[7] See "*Fixed-Mobile Substitution And Lessons For Broadband*", by Aniruddha Banerjee, Ph.D., http://www.accc.gov.au/content/item.phtml?itemId=793243&nodeId=7242ee699c361197b7dbeec507cf00d2&fn=Banerjee%20-%20Paper.pdf

QUESTION G3: Finally we would like to ask you to elaborate on the question of converging MTR and FTRs and the timeframe you envisage for this.

At the moment true costs of mobile termination are not clear, but (see M1 hereinafter) in Italy is at least clear that the incumbents TR (14.95 Eurocent/min as to Vodafone and TIM in 2003 and 10.0 Eurocent/min as of today) are well above their mobile termination costs (around 4 Eurocent, respectively, as of 2003 and even less today).

If NRA will impose the decrease of MTR in respect of cost orientation obligation, MTR will certainly converge towards the level of FTR, but there is no reason to presume that in a certainly timeframe FTR and MTR will (or should) be the same.

Again: instead of asking for the timeframe of converging FTR and MTR level, ERG should strongly encourage NRAs to ensure as soon as possible symmetry in the application of remedies: the use of symmetric cost analysis tools and methodologies to determine cost oriented TR for fixed and mobile operators (e.g. excluding marketing and access costs after a transitional entry period, as pointed out in the consultation document, page 90: "*harmonization of these methodologies between MT regulation and FT regulation could potentially induce a reduction of the existing asymmetry such that the remaining gap is justified by cost differences, leading to positive effects on competition between telecoms players, and ultimately on end-users*").

PART 2:FIXED CALL TERMINATION

QUESTION F1: How do you think termination should be regulated in a converging fixed mobile market?

Setting TR in a converging fixed-mobile market, NRAs should:

a) ensure harmonization and symmetry of cost analysis tools and methodologies between MT regulation and FT regulation;

b) ensure the application of cost oriented FTR and MTR on the basis of such harmonized and symmetric cost analysis tools and methodologies (and, therefore, apply cost accounting and accounting separation principles on a consistent manner to both mobile and fixed operators);

c) when, as occurred in Italy (see above, G1-G3) regulation did not ensure point (a) and (b), NRAs should prevent incumbents and/or early entrants in mobile network from getting advantages out of that; in such cases, NRA should amend competitive distortions caused by regulation itself, in order to ensure, either (preferably, in the interest of end users) with temporary and extraordinary measures, or, by maintaining existing regulatory barriers to the development of convergent services (e.g. the ones concerning numbering, MNP, etc.), a fair and level playing field for competition between fixed and mobile operators;

d) at the same time NRAs should guarantee equal opportunities for the provisions of convergent services also to fixed OAOs.

   As a matter of fact, given the network externalities described above (and the existence of high and non transitory entry barriers to the mobile market), NRAs should prevent unduly TR discrimination by fixed and mobile integrated operators with respect to their fixed networks competitors, by imposing to all SMP operators equality of access between their division and third parties.

For this purpose, since it would not be possible to impose, at an external level, the disaggregation of F-M convergent offers, NRAs should impose internally a sufficient level of transparency and cost accounting separation, in order to verify consistency between TR applied to competitors and (TR applied internally for) retail convergent services prices.

With regard to the last issue, AIIP has serious concern that abusive prices discriminations in termination rates will increase in a converging fixed mobile market.

Therefore, ERG should recommend NRAs to look out for discrimination and cross subsidies having in mind, for instance, that there is no reason why MTR should be different if the terminal is within a home zone or outside, given that the costs associated with the location of a mobile terminal in a MNO network are minimal compared to other relevant costs (or, in any case, that the same TR applied internally by MNO should be reserved to competitors).

QUESTION F2: Do you agree on the methodology and assumptions underlying the asymmetry index calculation?

For the above mentioned reasons, AIIP does not perceive asymmetry as something that should be compared and "indexed".

As a matter of fact the level of cost oriented termination various among operators and domestic markets (e.g. due to non homogeneous market shares and number of subscribers between incumbents and OAOs, timing of effective opening of the market, etc.). Therefore it is not possible and would make no sense to calculate such an index and, in any case, no conclusions could be drawn.

QUESTION F3: Do you think the list in paragraph 6.1 constitutes an exhaustive list of the possible reasons justifying the adoption of asymmetric tariffs?

As reasons for FTR asymmetry ERG list the following: lower economies of scale, incentives to invest, different network coverage, structure and topology, lower bargaining power.

AIIP believes that asymmetric FTR may be justified by any difference between the costs of operators not due to their productive inefficiency and any factors outside their control, included historically occurred advantages, resulting from regulation (the Italian incumbent for example has made the majority of its network investments in the course of time, in a monopoly regime, obtaining adequate remuneration; alternative operators, on the other hand, find themselves investing in a liberalized market with a greater market risk) or incumbent abuse of dominant position (e.g., in Italy, prices squeeze and interconnection discrimination practices were ascertained by the antitrust authority in case A351 and were also uphold by the Court).

AIIP highly disagree with ERG conclusion: "*In other terms, asymmetric FTRs in favor of OAOs have been interpreted by some NRAs as a form of entry assistance that may have long term benefits if they lead to an increase in the number of sustainable providers of fixed telecommunications services in the long run*".

The need of new entrants to recover their costs for network build-out, which have already been recovered by the incumbents does not imply any inefficiency. As a matter of fact:

- to face costs associated with lower market shares and lower scale economies does not mean to be a productively inefficient firm, and it should be considered that larger market share and larger scale economies need time to be reached (so that a reasonable time to reach an efficient scale should be recognize to any single competitor entering the market);
- to face costs associated with winning market share in a more mature market does not mean to be productively inefficient.
- to face higher marketing costs compared with the incumbent that can rely upon a well-established customer base, does not mean to be inefficient.
- to face network externalities and costs due to incumbents anticompetitive behaviors does not mean to be inefficient.

To consider all these costs is not a form of entry assistance introduced by NRAs to increase artificially the number of OAOs.

Contrary, in a paradoxical way, an assistance policy in favor of the incumbents would result from a regulatory approach not considering any more, from a certain moment, all these differences. Such a regulatory approach seems to suppose that the ideal number of operators to let enter the market has (or should have) already been reached. Such an approach would certainly create competitive distortions through regulation.

QUESTION F4: Do you agree on the fact that any entry assistance policy for the future based on higher OAOs' FTRs is likely to be less effective than in the past?

On the one end, AIIP disagree on the fact that allowing asymmetric TR is an entry assistance policy in favour of OAOs.

As stated above, it must be clear that higher OAOs FTRs are not an asymmetric regulatory measure adopted to encourage the development of new entrants, and imposing constraint on the "more efficient" incumbents to subsidize the "relative inefficiencies" of OAOs, with a sort of assistance policy (as ERG seems to consider them). Higher OAOs FTR are rather the result of the implementation of symmetry in remedies: as a matter of fact, "price control and cost accounting" obligations were imposed also to OAOs. Therefore regulation precluded OAOs to realize any access mark-up or extra profit which could result in an incentive to enter the market in a sort of entry assistance policy.

On the other end, AIIP has serious concerns that improper regulation could create a sort of assistance policy in favour of incumbents (and earlier OAOs).

As stated above, the ERG approach presuming that TR should become symmetric, may practically exclude from the market any new competitor and would artificially "crystallize" market structure. Moreover unduly competitive advantages in favour of the incumbents could result from delay in the proper implementation of obligations such as non discrimination, cost orientation, and separate accounting obligation, since this delay may have allowed firms to gain extra-profits which could become a competitive disadvantage for new entrants.

The ERG consultation document deems that: "*While in the past fixed telecom operators essentially provided a limited range of telephony services, in recent years operators have been able to use the same network to provide a wide range of services, including broadcasting and broadband Internet in addition to telephony. This means that revenues from termination services are proportionally likely to become less important to all operators, incumbents and OAOs alike*".

AIIP disagrees.

TR will remain a substantial part of revenues and source of large profits resulting in a significant source of cash-flow to the advantage of incumbents due to their persistent market shares (89,8 in Italy).

Moreover, regarding the provision of a wide range of services, by "bundle" offers, incumbents may better hide price discrimination policies in FTR between their internal division and competitors and have more opportunities to cross subsidies investments in NGN, broadband Internet, broadcasting, and access services (e.g. for Italy, clear evidences of such policies and the strategic role of bundles in exclusionary conduct, were acquired with the antitrust proceeding n. A351 – *Comportamenti abusivi di Telecom Italia*, November 2004, already uphold by the Court).

Indeed, it is unclear why lower economies of scale suffered by OAOs should be treated differently from the past. Even if fixed OAOs may enter in the national market operating on a regional or local basis (today as in the past), the problem of increasing scale (and scope) economies, which would lead to descending unit cost for increasing total production output persist, causing for new entrants a clear disadvantage relative to the incumbent.

QUESTION F5: Could you please provide a definition of the "efficient operator" NRAs should refer to in fixing FTRs? What are the costs an efficient operator would incur to provide termination services?

AIIP believes that in fixing FTR NRAs should principally refer to all incurred costs.

The risks considered by the economic theories mentioned in the consultation document, should not lead to abstractly predetermine the level of costs of an efficient operator.

Use a concept of "efficient operator" to determine the costs an efficient operator would incur to provide termination services could be very risky. The principal risk is to link the concept of efficiency and the costs of such an "efficient operator" to a certain technology (i) contrary to the fundamental principle of technological neutrality; (ii) regardless the fact that electronic communication industry is very dynamic from this point of view.

Contrary, it would be sufficient and proportionate to the scope of promoting efficiency (underlined by the economic theories mentioned in the consultation document) to simply impose to every provider a reasonable glide path of decreasing its TR, compatibly with its sustainable grow towards reaching an efficient scale.

AIIP would suggest the application of a regulation of "rate of return type", base on cost effectively sustained, with a "price cap" (x-%) which should ensure efficiency during time.

A periodical revision of OAOs costs and cost oriented TR is then necessary to ensure that efficiency gain are reversed on final customers.

QUESTION F6: Do you agree on the fact that OAOs should be as efficient as the incumbent?

To begin with, the above question moves from a wrong assumption.

There are no reasons to presume the incumbent productive efficiency and no reasons to presume OAOs less productive efficiency. There is not a direct relation between lower TR and productive efficiency, or higher TR and productive inefficiency.

In general, productive inefficiencies are more likely of incumbents, since they are also linked to past productive solutions, while new entrants naturally tend to productive efficiency as to be able to compete at the retail level with well established operators, acquire customers in a mature market, recover investments, etc.

AIIP agrees that price controls should not be related only to costs actually incurred, regardless of productive efficiency (see F5 above).

However to link price controls also to a certain concept of "efficiency" does not imply that any OAOs, could or should be as efficient as an incumbent in the misleading sense of having the same TR (see F3 above).

QUESTION F7: Do you agree on the fact that there are less reasons for fixed operators compared to mobile operators that justify the adoption of asymmetric tariffs?

AIIP strongly disagrees with this conclusion.

Even if fixed OAOs may enter in the (national) market on a regional or local basis (since national coverage obligations are limited to mobile networks) the problem of increasing scale (and scope) economies and high sunk costs persist, and cause for new entrants on fixed networks a clear disadvantage in relation to the incumbent.

As a matter of fact, sunk costs for coverage a certain area are higher in a fixed network than in a mobile network; moreover, marginal costs increase in fixed network whereas decrease in a mobile network.

In fact, a mobile network and service provider may progressively adequate the network capacity in the area of coverage to the increasing number of end users and traffic, with decreasing incremental costs, whereas fixed service providers can not do so and, therefore, initially face larger scale diseconomies.

To conclude, AIIP believes that the drivers for asymmetry indicated in answer to question M2 may be at play also on a fixed network. To the utmost, there could be less reasons justifying asymmetric regulation, not less reasons justifying asymmetric / non reciprocal FTR in fixed networks.

QUESTION F8: Do you agree on the fact that if all call termination charges were based strictly on incurred costs there would be a distortion of competition?

Call termination charges based on incurred costs would not distort competition. The risk to cause distortion of competition considered in the question is high below the risk to distort competition by impeding new entrants to recover their costs.

QUESTION F9: Do you agree on the fact that symmetric tariffs would allow to avoid transaction and regulatory costs?

The question is misleading.

Transaction and regulatory costs could not be a deterrent as long as there are reasons for imposing transparency, non discrimination, access/interconnection obligation, price control and cost accounting obligation, and accounting separation.

QUESTION F10: Do you agree on the fact that NRAs should reach symmetry in fixed termination tariffs within a reasonable period of time? QUESTION F11: Do you agree that it would be reasonable for NRAs to allow a transition period to move to symmetric FTRs? How long should this transition period be? QUESTION F12: In your opinion what criterion should NRAs adopt to set the glide path?

For all the reason above, according to AIIP NRA should not adopt a path towards symmetric and reciprocal TR (nor e a glide path, nor a prompt path).

The regulatory measures that the Commission (with ERG's plain endorsement) seeks to introduce may lead to serious and unrecoverable damages to market structure.

The Commission, ERG and NRA should rather concentrate to swiftly fill persisting regulatory gaps, achieving in the mostly short term the harmonization in cost accounting remedies and principle as well as in cost analysis tools and methodologies to determine cost orientated prices.

QUESTION F13: As the length of the glide path is a controversial point, in your opinion, should the time period to reach symmetry be the same for all NRAs or should each NRA determine it according to national circumstances?

See above. In any case, it appears of clear evidence that TR should be determine taking into account the market circumstances and, since market are still national wide, it would seem totally illogical to imagine a time period to reach the same reciprocal TR for all operators in all Member states.

QUESTION M1: Do you agree with the general principle promoting symmetry: "*Termination rates should normally be symmetric*"?

AIIP disagrees with the general statement that there should normally be a unique and reciprocal MTR.

Rather, there should be cost oriented MTR for all MNOs fixed according to same criteria and method set forth for FNOs and MNOs[8] harmonized for all European Countries (as a matter of fact, in presence of European pan-operators on either fixed or mobile markets or on both of the, any subsidy achieved in a Country might produce distortions on other Countries).

It is important to note that excessive prices could be due to monopoly extra-profits or productive inefficiencies.

By setting MTR, NRAs should prevent MNOs to benefit monopoly extra-profits and therefore determine cost oriented termination rates (in an harmonized manner).

In this regard hereinafter is described the Italian situation, where the Italian Competition Authority (ICA) has found by Decision no. 17131, A357 - *Tele2/Tim-Vodafone-Wind* (of August 3, 2007) that Telecom and Wind held an individual dominant position on the market of wholesale termination services on their own mobile networks and that, between 2001-1st half 2006, abused thereof by applying to their own commercial divisions technical and/or economic conditions for termination of on-net fixed to mobile ("F2M") calls which were more favourable than those applied to competitors[9].

The discriminatory practices imposed on their competitors by the two mobile operators, who also have licences to supply fixed network telephone services, was intended to exclude competitors both from:

(i) wholesale termination services, preventing the creation of a "secondary" market of termination services on mobile networks, alternative to interconnection (by means of refusal to negotiate wholesale agreements in order to terminate ad technical and/or economic conditions equal to the ones applied by MNOs to their commercial divisions and of deactivations of SIM used with the awareness of the MNOs in GSM gateways and of direct connections between PABXs and the MSC nodes of the relevant mobile network) and

[8] The general grounds for different TR between operators are explained in the first part of this document: according to AIIP, symmetry in MTR cannot be set as a general rule, irrespective from the date of entrance on the market by each operator. The fixing of a principle of symmetry in MTR, without any tempering would create a regulatory entry barrier and distort competition.

[9] It is noteworthy to underline that the final decision does not concern Vodafone just because the latter submitted commitments accepted by a separate decision according to which it was exempted from the procedure (Decision no. 16871, A357 - *Tele2/Tim-Vodafone-Wind*, of May 24, 2007), but as a matter of fact, many statements contained in the ICA's Statement of Objections concerned the same behaviours put in place by Vodafone. E.g.: "*between 2000 and September 2005, even Vodafone' business call rates [for on-net and internal calls], were well below the termination rates applied by Vodafone to competitors*"; more "*precisely, the following prices applied by Vodafone to business customers are below access and termination costs for such services [...] and it is noteworthy to underline that such prices are always below the mere termination costs*" (§§ 443-446).

(ii) the related retail market for F-M voice services for business customers, since such services were sold by the MNOs themselves at a price half of the wholesale termination fee, for an activity including access and transit in addition to termination.

<u>According to ICA's findings, the MNOs discriminatory and "price squeeze" practices were realized by selling retail mobile-to-mobile *on net* traffic (originated by their own clients and terminated on the same MNO network) at a price half than the wholesale tariff applied to competitors for the termination service alone</u>.

<u>This practices not be possible if the termination rates of such MNOs were set at real cost oriented levels.</u>

In some 2003 internal report (acquired by ICA during the preliminary investigations), Telecom:

(i) asserts that TR (14,95 €cent/min) were highly above its real costs, thanks to its strategies before the NRA and that the maintenance of TR above costs was a source for Telecom during 2003 of extra-revenues "*around [..] Mln €*"[10];

(ii) imputes the phenomena of shifting (through GSM Gateways) F2M traffic in to M2M traffic to "the difference between the F2M TR (14,95 cent/€) and the average price for on-net traffic (8 cent/€)" and estimates an effect on its 2003 termination revenues "amounting to about [*omissis*] Mln Euro" (see par. 135, Decision no. 17131, A357 above referred)[11].

It follows that:

(1) once recovered the network roll out costs, revenues from TR became for the incumbent MNOs an incredible source of extra-profits;

(2) <u>as a matter of fact Telecom TR for 2003 were set up to the maximum level of 14,95</u>

[10] "*la <u>strategia nei confronti del regolatore</u>, in relazione alla tematica fisso-mobile, <u>ha evitato l'imposizione di un prezzo massimo inferiore ai 14,95 €cent/min stabilite nel corso del 2003, sulla base delle risultanze dei dati di contabilità regolatoria</u>. In tal modo con il mantenimento di un valore minutario medio della terminazione* [allora fissato in via regolamentare in 14,95 eurocent/min] *<u>abbondantemente superiore ai costi reali di TIM</u>, si è preservata una delle maggiori fonti di ricavo per un operatore di telefona mobile; tale maggior ricavo è quantificabile in circa […] mln di euro per il solo esercizio 2003*" (see doc. 4.7 A357 proceeding, "*Bilancio regolamentare AR anno 2003*".

[11] "*Tuttavia, il crescente utilizzo nel 2003 di soluzioni tecniche che consentono la sostituzione del traffico F-M con quello M-M da parte non solo dei clienti aziendali, ma anche di altri operatori, comincia a destare preoccupazione nel gestore, che effettua una serie di studi volti a valutare l'impatto, in termini di ricavi, dell'utilizzo delle SIM box. Ciò si ricava dalla lettura congiunta di due documenti interni: il doc. 4.11, del 12 febbraio 2004, e il doc. 4.10, del 24 gennaio 2004. Più precisamene, il primo documento citato fornisce una misura dell'incremento di traffico da SIM Box, che è passato da* **[***omissis***]** *milioni di minuti/mese del gennaio 2002 a* **[***omissis***]** *milioni di minuti mese nel dicembre 2003 (doc. 4.11, pag. 4). La causa di tale fenomeno deriva dal "***DIFFERENZIALE TRA LA TARIFFA D'INTERCONNESSIONE F-M (14,95 CENT/€) E LA TARIFFA MEDIA ON-NET PER CLIENTI RESELLER PARI A 8 CENT/€…***", con un impatto per il 2003 di circa* **[***omissis***]** *milioni di euro in termini di minori ricavi da terminazione, a fronte di circa* **[***omissis***]** *milioni di minuti di traffico effettuato con SIM Box; tale valore è destinato a crescere nel 2004, anno nel quale l'impatto stimato in termini di minori entrate è pari a circa* **[***omissis***]** *milioni di euro, ipotizzando un volume di minuti mese pari a quello "DI USCITA 2003" di "CIRCA* **[***omissis***]** *MIL/MIN/MESE" (ivi, pag. 6)*".

Eurocenmt/min in spite of the fact that should have not exceeded 4 Eurocent/min (1/2 the final cost of on-net traffic, which includes access and transit, in addition to termination) and, therefore, today should be largely below 4 Eurocent/min.;

(3) the same is reasonably true as to Vodafone TR;

(4) the above extra-profits have been (ad are still being) used for on-net offers, causing distortion of competition in the F2M market and, eventually a Fixed-Mobile traffic substitution phenomena which result in a reduction of fixed network accesses and subsequent network diseconomies, which reduce fixed network operators cash flow for financing network investments and reducing digital divide in the broadband[12];

(5) more recently, the above extra-profits are used by the incumbents to subsidize convergent offers, thus further distorting the competitive environment of the market to the detriment of FNO;

(6) reasonably also the TR of many other MNO incumbents in Europe should be highly below the present (since the Italian MTR are higher, but not very far from MTR in other countries, as result from the ERG last MTR update snapshot – "ERG (07) 61 rev_1) and "*mobile terminating tariffs are in general more than 10 times as high as fixed terminating*" because the MNOs are achieving extra-profits.

It is noteworthy that recently:

(i) both ICA's decision were confirmed by the Administrative Court;

(ii) the Italian NRA decided to re-open markets 15 (Decision n. 168/07/CONS of April 19, 2007) and 16 (Decison no. 342/07/CONS of June 28, 2007) for their better regulation.

In the above described environment, imposing symmetric TR would certainly strengthen existing advantages for incumbent operators of fixed networks and early entrant mobile operators, since the latter have been allowed to fully recover costs for network build-out, in the initial phase, and, once completed the network roll-out, have also realized (abusive) extra-profits.

AIIP suggests that ERG and the EU Commission chose more carefully their advisors to guarantee their impartiality. AIIP has serious concerns on the impartiality of the economic theory refereed by ERG in the consultation documents. As a matter of fact Tommaso Valletti is, or has been, one of Vodafone advisor (e.g. a survey commissioned to it by Vodafone was submitted by the latter before the Italian Competition Authority) and in his "*Asymmetric regulation of mobile termination rates*" makes reference, among the others, to Littlechild, S., 2003 "*Price controls on mobile termination changes*" published in "*The Vodafone Policy Paper Series*".

Exception to take into account exogenous factors, not related to a late entrance:

QUESTION M2: Do you agree with the exception to take into account exogenous cost differences: "*asymmetry is only acceptable to take into account exogenous factors, outside the control of operators*"? The only example, which is not related to a late entrance, identified by

[12] See "*Fixed-Mobile Substitution And Lessons For Broadband*", by Aniruddha Banerjee, Ph.D., http://www.accc.gov.au/content/item.phtml?itemId=793243&nodeId=7242ee699c361197b7dbeec507cf00d2&fn=Banerjee%20-%20Paper.pdf

ERG is cost differences due to the spectrum licensing holdings. Can you identify other exogenous factors?

AIIP agrees on taking into account spectrum asymmetries as an exogenous factor.

QUESTION M3: Do you agree with the following principle: "*Assuming that cost differences due to different spectrum allocation are properly evaluated, they may justify an asymmetry*"?

AIIP agrees on the above and invites ERG to harmonize the criteria to assess such cost differences with objective factors (e.g.: population per Mhz, etc…)

Transitory exception to take into a significantly late entrance:

QUESTION M4: Do you agree with the following principle: "*If the level of competition in the mobile retail market asks for measures which create incentives for new network level entry or measures that strengthen the position of small new entrants, substantial differences in the date of market entry can justify an asymmetry for a transitory period*"?

AIIP agrees with the above.

QUESTION M5: Do you agree with the principle of keeping the level of asymmetry "*reasonable*"?

AIIP deems that first the concept of "reasonable" should be clarified. If this means "proportionate", AIIP may agree.

QUESTION M6: Do you agree with the fact that an initial level should be accompanied by a glide path towards symmetry?

As clarified above (see Introduction), there are a number of factors that may justify cost differences on a non transitory basis. Therefore, AIIP does not agree on the above.

QUESTION M7: Do you agree with the fact that national factors should be taken into account to evaluate the length of the transition period?

AIIP does not agree on a transitional period of asymmetry, for the above reason.

However, AIIP agrees that nationally factors should be taken into account, such as:

⇒ Number of years of late entry.

⇒ Market penetration when entered in the market.

⇒ Average churn rate in the market.

Transitory exception before MTRs are at cost, to limit distortions created by MTRs above costs:

QUESTION M8: Do you agree that in specific market circumstances (MTRs tariffs are significantly above MTR costs, there are high traffic imbalances between mobile operators and benefits of a transitory asymmetry outweigh any short term disadvantages of doing so), a temporary asymmetry may limit competitive distortions?

As clarified under answer to question M1, from MTRs not cost oriented would follow serious distortions which would affect the market much worse than any traffic imbalance.

QUESTION M9: Do you agree that NRAs should first try to set MTRs at costs?

AIIP agrees that cost oriented MTR should be THE priority to prevent distortions of competition, especially in convergent fixed and mobile communications markets.

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Best regards,

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