BoR (13) 04

**BEREC Opinion on**

**Phase II investigation**

**pursuant to Article 7a of Directive 2002/21/EC as amended by Directive 2009/140/EC:**

**Case CZ/2012/1392**

**Call termination on individual public telephone networks provided at a fixed location (market 3) in the Czech Republic**

**21 January 2013**

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# 1. EXECUTIVE SUMMARY

On 8 November 2012, the Commission registered a notification by the Czech Regulatory Authority, ČTÚ, concerning the control remedies on the wholesale market for call termination on individual public telephone networks provided at a fixed location.[1]

In the draft measure ČTÚ proposes to impose on Telefónica Czech Republic a.s. fixed termination rates that target pure BU-LRIC rates from 1 July 2013 in line with the Termination Rates Recommendation (Recommendation).

On 10 December 2012, the Commission sent a serious doubts letter opening a phase II investigation pursuant to Article 7a of Directive 2002/21/EC as amended by Directive 2009/140/EC. The Commission's doubts concern the non-imposition of appropriate termination rates by ČTÚ.

On the basis of the economic analysis set out in this Opinion, BEREC considers that the Commission's arguments in the serious doubts are not justified.

BEREC is of the opinion that the resulting price levels, as notified by ČTÚ, cannot be in itself a reason to have serious doubts. The NRA has to show that it has modelled FTRs in line with the Recommendation but it should not have to provide a justification why its FTRs differ from FTRs in other EU member states.

BEREC does not share the arguments put forward by the Commission used to express their serious doubts. In particular, the Commission noted that ČTÚ's modelled network is not NGN-based in its entirety. According to BEREC, the model used by ČTÚ is fully NGN-based.

The Commission concludes in its serious doubts that the rates are not set on the basis of the costs of an efficient operator. In order to assess if the conclusion about the modelling of an efficient operator could still be valid, BEREC checked whether other key elements of the methodology used by CTU are complying with the Recommendation. BEREC considers that three aspects of the methodology used by CTU with regard to modelling an efficient operator could validate the conclusion of the Commission.

BEREC recommends that these three elements of the methodology need to be examined more closely by ČTÚ and the Commission before the final decision. First, the efficiency level of the wholesale billing costs should be double checked taking into account international incoming and retail traffic to consider the correct economies of scale. Second, the way the peak and off-peak tariffs are calculated does not reflect empirical demand. Third, the exclusion of international incoming traffic in the calculation of the incremental costs can neglect economies of scale. These elements may explain differences in outcome with the countries mentioned by the Commission.

BEREC considers that serious doubts postpone the implementation of the proposed FTRs. The FTRs proposed by ČTÚ reduce the current termination rates already by more than 75%. The implementation of the proposed FTRs contribute therefore already to a large extent to

[1] At the same date ČTÚ also notified price related remedies on the markets for voice call termination on individual mobile networks in the Czech Republic (case CZ/2012/1393). As the serious doubts do not concern these markets they are left outside this opinion.

the objectives laid down in Article 8 of the Framework Directive and Article 13(2) of the Access Directive. BEREC therefore recommends the Commission to reconsider the serious doubts and suggests examining in close cooperation with ČTÚ the wholesale billing costs, the calculation of the peak and off-peak tariffs and the exclusion of international incoming traffic in order to assure that an efficient operator is modelled.

## 2. INTRODUCTION

On 8 November 2012, the Commission registered a notification by the Czech Regulatory Authority, ČTÚ, concerning the control remedies on the wholesale market for call termination on individual public telephone networks provided at a fixed location. On 14 November 2012, a request for information (RFI) was sent to ČTÚ, and a response was received on 19 November 2012. On 21 November 2012 a supplementary RFI was sent to ČTÚ, and a response was received on 26 November 2012.

The Commission initiated a phase II investigation, pursuant to Article 7a of Directive 2002/21/EC as amended by Directive 2009/140/EC, with a serious doubts letter on 10 December 2012.

In accordance with the BEREC rules of procedure, the Expert Working Group (EWG) was established on 13 December 2012 with the mandate to prepare an independent BEREC opinion on the justification of the Commission's serious doubts on the case.

On 17 December 2012 the EWG sent a first list of questions to ČTÚ. Answers were received from ČTÚ on 18 December 2012. On 17 December 2012 the EWG also received ČTÚ's view on the serious doubts letter of the Commission from 10 December 2012.

On 19 December 2012 the EWG met in Den Haag. During this meeting the EWG held a meeting with ČTÚ to gather further information and clarification in response to the RFI and to subsequent additional questions. The objective of the EWG was to reach clear conclusions on whether or not the Commission's serious doubts are justified.

In total five sets of questions were sent to ČTÚ. Answers from ČTÚ were all received within three days.

The Commission sent additional questions to ČTÚ on 18 December 2012, and the Commission and the EWG received the answers on 21 December 2012.

A draft opinion was finalized on 14 January 2013 and presented to the BEREC Board of Regulators for comments. The final opinion was presented and adopted by a majority of the BEREC Board of Regulators on 21 January 2013. This opinion is now issued by BEREC in accordance with Article 7a(3) of the Framework Directive.

# 3. BACKGROUND

**Previous notifications**

In its second market review of the markets for wholesale call termination on individual public telephone networks provided at a fixed location ČTÚ designated 24 operators as having SMP. A full set of remedies was imposed on Telefónica O2. With regard to other operators ČTÚ proposed to impose only transparency and non-discrimination obligations. The Commission commented and invited ČTÚ to impose a cost orientation as well as an access obligation on all SMP market players.

ČTÚ notified the price related remedies applicable to fixed termination rates applied by Telefónica O2 separately. The fixed termination rates (FTRs) were based on a LRIC methodology. The Commission had no comments.

**Current notification**

In the current notification ČTÚ proposed to impose on Telefónica Czech Republic a.s. a two staged glide path to be applied from 1 January 2013 and from 1 July 2013 respectively. ČTÚ intends to impose fixed termination rates that target pure BU-LRIC rates from 1 July 2013 at the following levels:

| Price cap (€-cents per minute) | | From 1 January 2013 | From 1 July 2013 |
|---|---|---|---|
| Local exchange (HOST) | Peak | 0.75 | 0.28 |
| | Off-peak | 0.39 | 0.16 |
| Last transit exchange | Peak | 0.83 | 0.31 |
| | Off-peak | 0.43 | 0.16 |

**Commission's comments**

The Commission has the following comments with regard to the notification of the FTRs:

1. *Non-imposition of effective remedies on all SMP market players and the need to carry out new analyses of the market for termination on fixed networks*

The Commission disagrees with the approach that the proposed regulation concerns only one fixed network operator. The approach taken by ČTÚ has the ultimate effect of continued asymmetry in price regulation of SMP operators. As the scope of the notification concerns only the amendment of price related remedies which ČTÚ has already imposed earlier the Commission cannot proceed with the opening of a phase II investigation. The Commission notes that the last market analysis was carried out by ČTÚ in 2009. The Commission urges ČTÚ to carry out and notify a new market analysis of the markets for fixed termination;[2]

[2] Although formally outside the scope of this opinion, BEREC agrees with this comment that in general the minimum remedy for SMP operators in the individual termination markets is price regulation based on the pure LRIC cost standard.

2. *Implementation of the termination rates recommendation*

The Commission notes that the proposed measures are not fully in line with the Termination Rates Recommendation according to which NRAs should ensure termination rates at the cost efficient (pure LRIC) level by 31 December 2012. The Commission considers that the proposed delay to 1 July 2013 may exceptionally be acceptable in this case. The Commission invites ČTÚ to consider cost-efficient termination rates already as of 1 January 2013;

3. *Need to notify the cost model used for the calculation of the fixed termination rates to the Commission*

The Commission requests ČTÚ to notify the cost model used for the calculation of the fixed termination rates.

**Commission's serious doubts**

The Commission expresses serious doubts for the following principal reason:

***"The non-imposition of appropriate fixed termination rates:***

*Regarding the proposed FTRs, the Commission observes that ČTÚ proposes to impose price caps applicable to termination segmented for interconnection at (i) local exchange (host) and for interconnection at (ii) last transit exchange. Secondly, the Commission would also like to stress that, even though ČTÚ explains that FTRs were calculated on the basis of a pure BU-LRIC cost model which ČTÚ failed to notify to the Commission, the proposed rates between 0.16 €-cents and 0.31 €-cents per minute are approximately two times higher than in other EU Member States where a pure BU-LRIC methodology is used.*[3]

*The Commission highlights that pursuant to one of the core regulatory principles enshrined in Article 8(5)(d) of the Framework Directive, NRAs are required to promote efficient investment and innovation in new and enhanced infrastructures. It is on that basis that any cost model imposed should be based on efficient technologies available in the time frame considered by the model. Therefore the core part considered for fixed networks should in principle be next generation-network based.*

*The Commission has serious doubts that ČTÚ conforms to the mandatory principles under Article 8(5)(d) of the Framework Directive by imposing such price caps to termination markets which are segmented for interconnection at (i) local exchange (host) and for interconnection at (ii) last transit exchange. The Commission stresses that, according to ČTÚ's explanation, it decided to amend the cost model, which ČTÚ failed to notify to the Commission, during a national public consultation by introducing several changes to the definition of the input data, so that the model can, in ČTÚ's words, better reflect the reality, which is the fact that the SMP operator has not introduced the NGN technology to full extent.*

[3] In France such rate is 0.080 €-cents/min, in Ireland such rate is 0.098 €-cents/min, in Malta such rate is 0.044 €-cents/min and in Denmark such rate is 0.060 €-cents/min in peak time and 0.032 €-cents/min in off-peak time.

*Thus, ČTÚ failed to impose price caps that would consider next-generation-network based efficient technologies in its entirety, necessary to model the costs of an efficient operator as required by a BU-LRIC methodology.*

*Moreover, the Commission has serious doubts that the proposed FTRs conform with Article 13(2) of the Access Directive, which requires NRAs to ensure that any cost recovery mechanism or pricing methodology that is mandated serves to promote efficiency and sustainable competition and maximise consumer benefits while NRAs may also take account of prices available in comparable competitive markets, and would not be in line with Article 8(2) of the Framework Directive, which requires that NRAs should ensure that users derive maximum benefits in terms of price, choice and quality, and that there is no distortion or restriction of competition.*

*In this respect, the Commission points out that the model used by ČTÚ, which ČTÚ failed to notify to the Commission, does not ensure that rates are set on the basis of the costs of an efficient operator and therefore does not ensure that it will serve to promote efficiency and sustainable competition and maximise consumer benefits.*

***Creation of barriers to the internal market***

*The Commission considers that excessive prices for FTRs in the Czech Republic can negatively impact the ability of operators to offer pan-European connectivity to their retail (business) customers.*

*The Commission stresses the need to bring all termination rates towards an efficient level in a transparent and predictable manner.*

*In light of the above considerations, the Commission considers, at this stage, that the draft measure would create barriers to the internal market.*

***Conclusion***

*The Commission observes that ČTÚ's notification does not meet the policy objectives and regulatory principles enshrined in Article 8 of the Framework Directive, and cannot be considered to be in line with Articles 8(5)(d) of the Framework Directive and 13(2) of the Access Directive. Hence, the Commission has serious doubts that ČTÚ's proposal on FTRs can be justified in light of the objectives laid down in Article 8 of the Framework Directive, and in particular the objectives of promoting competition and user benefits and ensuring that there is no distortion or restriction of competition in the electronic communications sector, pursuant to Article 8(2) of the Framework Directive and believe, at this stage, that the draft measures would create barriers to the internal market."*

## 4. ASSESSMENT OF THE SERIOUS DOUBTS

On 10 December 2012, the Commission sent a serious doubts letter opening a phase II investigation pursuant to Article 7a of Directive 2002/21/EC as amended by Directive 2009/140/EC.

BEREC assesses the serious doubts in three parts. First, BEREC analyses the remarks of the Commission with regard to the observed price levels. Second, BEREC analyses the remarks of the Commission with regard to the methodology used to model the efficient operator. Third, BEREC analyses if the proposed FTRs create barriers to the internal market.

**The observed price levels**

*Concerns of the Commission*

The Commission observes that the proposed rates between 0.16 €-cents and 0.31 €-cents, calculated on the basis of a pure- BU-LRIC cost model, are approximately two times higher than in other EU-member states:

- France: 0.08 €-cents/min;
- Ireland: 0.098 €-cents/min; [4]
- Malta: 0.044 €-cents/min;
- Denmark: 0.06 €-cents/min in peak time and 0.032 €-cents in off-peak time.[5]

*Views of ČTÚ*

To EC's request to explain differences in FTRs ČTÚ responded that it is familiar with its own FTR calculations but not with FTR calculations in other member states and that the EC perhaps has the information needed to make the comparison between different member states. ČTÚ remarks that OPTA notified in 2010 pure BU-LRIC FTRs of 0.36 €-cents. In this light ČTÚ does not find its FTRs to be exceptionally high.

The understanding of ČTÚ is that the goal of the EC is to harmonise the methodology rather than prices (contrary to the roaming prices regulation). ČTÚ cannot consider higher FTRs per se as a proof demonstrating inconsistency with the Recommendation.

Finally, ČTÚ mentions that the difference in FTRs seems huge but is hardly perceivable for the final user.

*BEREC's Assessment*

According to Article 19 of the Framework Directive, NRAs should take utmost account of the Commission's Recommendations, including the Termination Rates Recommendation. This Recommendation provides a methodology to model an efficient operator.

BEREC considers that the Recommendation does not require the achievement of a certain level of termination rates but recommends a methodology to model an efficient operator.

BEREC is therefore of the opinion that the termination rates in other countries in itself cannot be used to motivate serious doubts by the Commission. The judgement by the Commission should be limited to the methodology implemented by ČTÚ. This methodology should be

[4] Fixed Termination Rates (FTRs) listed for Ireland are those that apply in the period 1 July 2013 to 30 June 2014. These FTRs are to fall to 0.085 €-cent in the period 1 July 2014 to 30 June 2015 and to 0.072 €-cent in the period 1 July 2015 to 30 June 2016.

[5] BEREC notes that the values for Denmark are not correct because a setup fee at a level of 0.063 €-cent per call is charged. In a usual case of a call duration of 2 minutes the value is 65 per cent higher than reported by the Commission.

checked against the methodology laid down in the Recommendation. While the NRA has to show that it has modelled FTRs in line with the Recommendation it should not have to provide a justification why its FTRs differ from FTRs in other EU member states. However the Commission should be provided with sufficient transparency regarding measures notified by NRAs in order to make its assessment under the article 7/7a process.

This does not imply that an NRA cannot learn from the termination rates in other EU member states. Indeed, termination rates comparison can be a tool for a NRA to check the consistency of its results or according to Article 12 of the Recommendation indeed be employed in establishing a benchmarking methodology set for termination rates. [6] In particular, a higher outcome than in other member states can be motivation for the NRA to double check the input values and hypothesis of the model taking into account that, according to the methodology in the Recommendation, an efficient operator is modelled.

However BEREC notes that differences can be found not only between the rates set by ČTÚ and other benchmarked NRAs but also among the rates of the benchmark countries. For instance, rates set for France and Ireland are also approximately two times higher than the rates in Malta.

In this regard it should also be noted that the number of benchmark countries is low as to date only four countries set FTRs based on the recommended pure BU-LRIC approach.

It should also be taken into account that there can be differences between member states in certain input parameters of the BU-LRIC model (e.g. fixed penetration rate, spread of demand, modelled traffic, asset prices, operational costs), which can affect the final result.

If this examination leads to the conclusion that the methodology used is in line with the Recommendation BEREC is of the opinion that the FTRs are in line with Article 8(5)(d) of the Framework Directive and Article 13(2) of the Access Directive and can be justified pursuant to Article 8 of the Framework Directive, and in particular Article 8(2).

**Methodology used to model an efficient operator**

*Concerns of the Commission*

The Commission has serious doubts that the proposed FTRs are in line with Article 8(5)(d) of the Framework Directive and Article 13(2) of the Access Directive and cannot be justified pursuant to Article 8 of the Framework Directive and in particular Article 8(2).

The Commission points out that the model used by ČTÚ does not ensure that rates are set on the basis of the costs of an efficient operator and therefore does not ensure that it will serve to promote efficiency and sustainable competition and maximize consumer benefits. ČTÚ failed to impose price caps that would consider next-generation-network based

[6] According to the Recommendation a benchmark is appropriate where an NRA is not in a position, in particular due to limited resources, to finalise the recommended cost model in a timely manner (prior to July 2014) and would be objectively disproportionate for those NRAs with limited resources to apply the recommended cost methodology after this date.

technologies in its entirety, necessary to model costs of an efficient operator as required by a BU-LRIC methodology.

The Commission notes that price caps are segmented for interconnection at (i) local exchange and for interconnection at (ii) last transit exchange. The Commission also stresses that, according to ČTÚ's explanation, it decided to amend the cost model, during a national public consultation by introducing several changes to the definition of the input data, so that the model can better reflect the reality, which is the fact that the SMP operator has not introduced NGN-technology to full extent.

*Views of ČTÚ*

ČTÚ has the conviction that both the methodology and the cost model are in compliance with the Recommendation. The EC has not provided evidence pointing to incorrect application of the recommended methodology.[7]

ČTÚ states that the changes in the model that the Commission is pointing at were not made during the national consultation but in the process before. The fact that the SMP operator has not introduced NGN to a full extent has not led to changes in the NGN topology or equipment modification. The network modelled is still full NGN.

ČTÚ has clarified that it changed some input parameters during the national consultation:

- ČTÚ added software prices into prices of network components – this change was expected in advance as the SMP operator had difficulties with reporting these costs and finally did so during the national consultation;
- From the billing costs ČTÚ excluded capacity dedicated for traffic in mobile network;
- SMP operator reported corrected number of minutes of transit traffic;
- SMP operator demanded adjustment of the cable length so that it reflected the real state. Taking into account rather small difference between optimal value (increase by 25 %) and the fact that the impact on the FTR was practically zero, ČTÚ complied with this request.

*BEREC's Assessment*

BEREC assesses evidences leading to Commission conclusion, ie that rate are not set on the basis of an efficient operator. First, BEREC will assess if it supports the arguments put forward by the Commission that the model is not NGN-based. Second, BEREC analyses whether other key elements of the methodology used by CTU are in line with the Recommendation, and could lead to the conclusion of the Commission that termination rates are not set on the basis of an efficient operator.

1. *Assessment of NGN-modelling*

The Commission underpins its serious doubts saying that ČTÚ did not model NGN in its entirety. BEREC notes that the Commission does not specify in what way the model is not

[7] ČTÚ stated that hypertext links to both the precise methodology and the BU-LRIC cost model were given in the reasoning part of the draft price decision making them thus logical and factual part of this measure.

NGN-based. BEREC has requested ČTÚ for information about their model. ČTÚ has provided BEREC with this information.

BERECs assessment concluded that ČTÚ's model is based on NGN technology and its topology reflects a certain level of efficiency. BEREC is also of the opinion that a network with two layers of interconnection points, respectively with two different interconnection fees, is not in contradiction with NGN. It is also no problem to use routing factors to determine the pure-LRIC for different levels of interconnection fees.

It might be that certain network elements are reflecting national specificities (such as MSAN construction, number of POIs, etc.), but BEREC does not consider these to be inconsistent with a NGN topology. In particular, the modelled NGN-network might appear a bit oversized in its core network (number of nodes) but is nevertheless a feasible design, and the analysis of ČTÚ also shows that the outcome of the model is not very sensitive to the size as most of these costs are not incremental.

The Commission also refers to changes by ČTÚ in the model during the national consultation. ČTÚ confirmed to BEREC that it did not change its model during the national consultation, but during the construction phase of the model. However even these changes made during the construction phase of the model did not lead to alteration of NGN-based topology of the modelled network. ČTÚ also clarified that they changed some of the input parameters after the national consultation (see above). According to BEREC the methodology in the final model version shows that it is NGN-based and the changes in the input parameters made during the consultation have not led to a deviation from this principle.

In addition it is in line with the Recommendation which states that "*the core part of both fixed and mobile networks could in principle be Next-Generation-Network (NGN)-based*".

BEREC therefore does not support the arguments the Commission used to express its serious doubts, i.e. that ČTÚ did not model NGN in its entirety. BEREC is of the opinion that the used model is NGN-based and the used methodology for that is in line with the Recommendation with regard to this aspect.

### *2. Assessment of other elements of the methodology*

The Commission concludes in its serious doubts that the rates are not set on the basis of the costs of an efficient operator. In order to assess if the conclusion about the modelling of an efficient operator could still be valid, BEREC checked whether other key elements of the methodology used by ČTÚ are complying with the Recommendation and especially if ČTÚ modelled an efficient operator. BEREC concludes that the model appears to follow the Recommendation with respect to:

- current costing;
- modelling of efficient technologies (NGN-based);
- calculation method incremental costs;
- demarcation of traffic-related and non-traffic-related costs;
- use of economic depreciation.

BEREC did not check if every individual parameter of the model reflects an efficient operator, but important input parameters such as mark-ups for OPEX and depreciation periods seem reasonably in line with expected values.

BEREC has three remarks with regard to the methodology used by ČTÚ and especially the modelling of an efficient operator. These remarks imply that the conclusion of the Commission could be valid. These remarks concern the:

a) level of the wholesale billing costs;
b) calculation of the peak and off-peak tariffs;
c) exclusion of international incoming traffic.

a) <u>Level of wholesale billing costs</u>

BEREC received information from ČTÚ on the breakdown of the incremental costs. The wholesale billing costs (IC-billing) consist of a very substantial part of the total incremental costs (**[confidential:** XXX**]** per cent), and represent on average a price of **[confidential:** XXX**]** €-cents per minute. The wholesale billing system encompasses the infrastructure from traffic data collection to invoicing and payment monitoring in particular hardware and software required to:

- collecting and processing wholesale billing records;
- warehousing of wholesale traffic data;
- invoicing of wholesale customers.

The level of the wholesale billing costs is an important parameter in the model. BEREC assumes that these costs explain to a large extent the differences in outcome with the countries mentioned by the Commission. The wholesale billing costs seem also high compared to the wholesale billing costs included in the MTRs notified by ČTÚ.[8] The modelled billing system seems only to include wholesale traffic, whereas including the international incoming traffic and retail traffic[9] in the same billing system could lead to economies of scale and therefore to lower billing costs per minute.[10]

On the other hand, BEREC stresses that the Commission accepted a notification by Spain with higher costs for MTR.[11]

BEREC would therefore advice to double check this input value of the model before publishing the final decision in order to examine if the correct economies of scale are taken into account and according to the methodology laid down in the Recommendation, an efficient operator is modelled for the wholesale billing costs.

[8] For MTR wholesale billing costs are modelled as a very tiny mark-up of **[confidential**: XXX**]** per cent on MTRs of 1.06 €-cent per minute.
[9] Taking into account retail services does not impose including the costs for generation of retail invoices. Only joint cost of technical pre-systems like collecting, storing and mediation of traffic tickets (CDR, Call Detail Record) have to be considered.
[10] BEREC has calculated based on data of ČTÚ the ratios between the incremental and the average cost of different network elements (access/locale/transit nodes, transmission systems between the different network levels, soft switch, MGW-POI and IC-billing-). The variability of all cost elements are in a reasonable range, except the ratio of IC-billing.
[11] Case: ES 2012/1314. The MTRs in this Spanish case include a mark-up of 0.35 €-cent/min for interconnection commercial costs.

In this regard, BEREC also stresses that the assessment of wholesale commercial costs varies among countries. As the incremental network costs for fixed network are low, the incremental wholesale commercial costs can represent a substantial proportion of the whole termination rate cost. This question would benefit from further investigations made by BEREC.

b) Calculation of the peak and off-peak tariffs

ČTÚ’s model provides an average incremental cost price for each interconnection level irrespective of the time of day for interconnection at (i) local exchange and for interconnection at (ii) last transit exchange.[12] Then ČTÚ uses these cost prices as well as retail prices to calculate the peak and off-peak wholesale tariffs for both interconnections at local and transit exchange. This calculation is based on an assumption regarding the volume of peak and off-peak traffic.

BEREC considers the approach chosen by ČTÚ as acceptable. The regulatory objective behind the idea setting different wholesale fees for peak and off-peak time is that the spread should guarantee an equal margin between retail and wholesale tariffs at peak and off-peak times.

Nevertheless, the resulting average tariff is sensitive to the assumption made by ČTÚ regarding the share of peak and off-peak traffic. If in reality the share of peak traffic is higher than ČTÚ assumed in the calculation the average tariff will rise and be higher than the average incremental cost price from the bottom up cost model.

BEREC is of the opinion that this is the case in ČTÚ’s model as the real share of peak traffic is higher than the parameter used by ČTÚ. BEREC therefore would advise ČTÚ to use a parameter set that is in line with the empirical demand regarding the volume of peak and off-peak traffic.

c) Exclusion of international incoming traffic

ČTÚ’s calculated incremental costs represent the incremental costs of termination traffic originated in Czech Republic and do not contain international incoming traffic that is terminated Czech Republic. According to BEREC this would probably lead to higher incremental costs per minute because of neglecting economies of scale. Also this might not reflect the size of the increment as defined in the Recommendation, i.e. the wholesale termination to third parties, irrespective of the location of origination

BEREC would therefore advise ČTÚ to analyse if their model outcome is sensitive to the exclusion of international incoming traffic.

**Creation of barriers to the internal market**

*Concerns of the Commission*

[12] According to ČTÚ´s explanation this terminology corresponds to the current PSTN netwok while the BU-LRIC cost model sets interconnection prices on the local and core IP router.

The Commission considers that the draft measure would create barriers to the internal market. Excessive prices for FTRs can negatively impact the ability of operators to offer pan-European connectivity to their retail (business) customers.

*Views of ČTÚ*

ČTÚ takes the view that it has set FTRs in full compliance with the Recommendation and thus at an efficient level.

*BEREC's Assessment*

BEREC concluded before that it did not support the arguments of the Commission to express serious doubts. Following this line BEREC does not support the arguments of the Commission that the FTRs create barriers to the internal market based on the elements put forward by the Commission.

However, BEREC made other remarks with regard to the methodology used by ČTÚ, which BEREC suggests to examine more closely.

## 5. CONCLUSIONS

On the basis of the economic analysis set out in section 4 above, BEREC considers that the Commission's arguments in the serious doubts regarding the draft decision of the Czech Regulatory Authority on the non-imposition of appropriate fixed termination rates - as expressed in the EC's letter to ČTÚ of 10 December 2012 – are not justified.

BEREC is of the opinion that the resulting price levels, as notified by ČTÚ, cannot be in itself a reason to have serious doubts. The NRA has to show that it has modelled FTRs in line with the Recommendation but it should not have to provide a justification why its FTRs differ from FTRs in other EU member states.

BEREC does not share the arguments put forward by the Commission used to express their serious doubts. In particular, the Commission noted that ČTÚ's model network is not NGN-based in its entirety. According to BEREC, the model used by ČTÚ is fully NGN-based.

The Commission concludes in its serious doubts that the rates are not set on the basis of the costs of an efficient operator. In order to assess if the conclusion about the modelling of an efficient operator could still be valid, BEREC checked whether other key elements of the methodology used by CTU are complying with the Recommendation. BEREC considers that three aspects of the methodology used by CTU with regard to modelling an efficient operator could validate the conclusion of the Commission.

BEREC recommends that these three elements of the methodology need to be examined more closely by ČTÚ and the Commission before the final decision. First, the efficiency level of the wholesale billing costs should be double checked taking into account international incoming and retail traffic to consider the correct economies of scale. Second, the way the peak and off-peak tariffs are calculated does not reflect empirical demand. Third, the exclusion of international incoming traffic in the calculation of the incremental costs can neglect economies of scale. These elements may explain differences in outcome with the countries mentioned by the Commission.

BEREC considers that serious doubts postpone the implementation of the proposed FTRs. The FTRs proposed by ČTÚ reduce the current termination rates already by more than 75 per cent. The implementation of the proposed FTRs contribute therefore already to a large extent to the objectives laid down in Article 8 of the Framework Directive and Article 13(2) of the Access Directive. BEREC therefore recommends the Commission to reconsider the serious doubts and suggests examining in close cooperation with ČTÚ the wholesale billing costs, the calculation of the peak and off-peak tariffs and the exclusion of international incoming traffic in order to assure that an efficient operator is modelled.

In general, BEREC considers that the assessment of wholesale commercial costs in line with the Recommendation would benefit from further investigation by BEREC.