# Review of the price control for wholesale on-island leased lines: Guernsey

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## Final Decision and Response to Consultation and Draft Decision

**Document No: CICRA 15/16**

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# Executive summary

Following the publication of its Final Decision on the Business Connectivity Market Review in October 2014, the GCRA undertook to review the price control which applied to the wholesale market for on-island leased lines, where Sure had been found with Significant Market Power (SMP). The GCRA published a Consultation and Draft Decision in March 2015. Having considered carefully the responses received from stakeholders, the GCRA now sets out its definitive position on the structure and implementation of the price control.

The GCRA notes that the ultimate goal of implementing a price control is to produce prices which replicate as much as possible those expected in an effectively competitive market. The implementation of a price control should encourage and protect efficient market entry and investment, and should ultimately benefit the end-user. The GCRA recognises that while price is highly important to retail customers, so too is quality of service, choice and investment in new products and services.

With these objectives in mind, the GCRA considered options as to how the price control may best be structured and implemented.

The GCRA has emphasised throughout the consultation process the fairness of the principle that prices charged to end-users should be related to the costs of supplying products and services. This Final Decision concludes that the most appropriate and proportionate means of achieving this is to put in place a retail minus price control, with supporting obligations which will establish clear rules about how wholesale on-island leased lines are to be supplied by Sure, and how Sure is to demonstrate that they are supplied in a way which complies with all of its obligations. The control will be set on an ex ante basis, will apply to all wholesale on-island leased lines, and will oblige Sure to make a wholesale equivalent available of all of its retail offers. The control will be set at retail minus 20%.

The supporting remedies set out by the GCRA include a requirement for Sure to provide a regular compliance statement which will facilitate increased transparency around pricing and costs of wholesale and retail leased lines.

The price control period will be aligned with the market review cycle, so that the retail minus price control will take effect with the adoption of this Decision, and will be subject to review as part of the next review of business connectivity.

# 1. Introduction

## 1.1 Background

The GCRA published its Final Decision on the Business Connectivity Market Review (BCMR) in Guernsey on 1 October 2014[1]. The BCMR concluded that Sure continues to hold Significant Market Power (SMP) in the market for on-island wholesale leased lines in Guernsey, but not in the market for off-island wholesale leased lines, and not in the market for retail leased lines. The GCRA proposed a set of remedies to be imposed on Sure to address the finding of SMP, and one of these was that a price control continues to be necessary in the wholesale market for on-island leased lines, as a necessary and proportionate remedy.

In March 2015, the GCRA published its Consultation and Draft Decision[2] on the review of the price control in the wholesale market for on-island leased lines. The review considers the market in Guernsey. The JCRA is undertaking a parallel review in Jersey, and the consultations have proceeded simultaneously.

CICRA received seven responses to its consultations on wholesale leased lines (CICRA 14/41 & 14/42), four of which related to Guernsey or to pan channel island issues, and would like to thank the respondents for their input to this process.

## 1.2 Structure of this document

This document constitutes a Final Decision (FD). The document sets out the conclusions which the GCRA has reached, having taken full account of responses to the Consultation and Draft Decision, and having carried out further research to ensure it has fully addressed respondents' points. The document contains summaries of particular points raised to illustrate the GCRA's reasoning.

This document broadly follows the structure of the March Consultation and Draft Decision, and is organised around the questions that were posed in that consultation. It is structured as follows:

Section 2: sets out options for the basis of the control;

Section 3: examines possible ways of structuring the control and discusses issues around the implementation of the control;

Section 4: contains the Final Decision.

[1] Document No CICRA 14/49
[2] Document No CICRA 15/07

Annex 1 outlines the legal requirements and licensing framework underpinning the market review;

Annex 2 is a glossary.

# 2. Basis of the control

## 2.1 Objectives of the price control

***The GCRA's Consultation and Draft Decision proposals and questions***

In the Draft Decision, the GCRA noted that the ultimate goal of implementing a price control is to produce prices which replicate as much as possible those expected in an effectively competitive market. The implementation of a price control should encourage and protect efficient market entry and investment, and should ultimately benefit the end-user.

For the operator, cost recovery is a central principle. Operators must be able to recover costs which have been efficiently incurred, and to receive an appropriate return on invested capital. The purchaser in the wholesale market for on-island leased lines is always an 'Other Licensed Operator' (OLO), and the price control should be set in such a way that pricing does not act as a barrier to an OLO's ability to enter and compete effectively in the market. However, the eventual beneficiary of the price control should be the end-user – the retail customer. The GCRA recognises that while price is highly important to retail customers, so too is quality of service, choice and investment in new products and services. The GCRA's assessment of possible approaches and methodologies has been undertaken with these principles at the forefront, in particular the interests of end-users.

The GCRA set out its view in the Draft Decision that the principle that prices charged to end-users should be related to the costs incurred in supply is reasonable and fair, both to operators and to customers. It is important also that the market functions in a way which facilitates competition within the retail market and encourages on-going investment by all operators in telecommunications infrastructure and services, so that high quality communications services are available to Guernsey customers.

## 2.2 Options

***The GCRA's Consultation and Draft Decision proposals and questions***

In the Draft Decision, the GCRA considered three options as mechanisms for setting price controls in the wholesale on-island market for leased lines in Guernsey. The GCRA's aim was to find a mechanism which has the desired outcome of achieving retail prices which are similar to those which would prevail in a competitive market, and which are fair and reasonable, both for the customer and for the supplier. The GCRA expressed a wish to achieve this in a way which is pragmatic, proportionate and implementable in practice.

The GCRA's view in the Draft Decision was that **benchmarking** is not sufficiently robust as a means of setting prices for services subject to this Decision. While benchmarking can provide comparative examples which may be useful indicators of any anomalies between pricing in Guernsey and pricing in other jurisdictions, the complexity of the products means that comparisons are not valid without a consideration of context.

The GCRA took the view that, in principle, relating prices to underlying costs would be reasonable and fair, both to operators and to customers. However, the GCRA's prime concern with **cost orientation** as a remedy (as opposed to a principle) was that it would be likely to be a resource-intensive remedy for both operators and the regulator, one which would take some time to implement, and one where the ultimate benefit for end users is not guaranteed. The GCRA was also concerned that a remedy based on cost modelling may not be sufficiently supportive of investment in infrastructure and services, and it noted that Ofcom had come to a similar conclusion in its review of the business connectivity market in the UK.

The GCRA took the view that one of the major advantages of a **retail-minus** approach is that it would strengthen the competitive environment by allowing market entrants to compete efficiently. However, a disadvantage of the retail minus approach is that it relies on competitors actively seeking to compete and grow market share. The GCRA noted that market entrants (notably JT) had made considerable inroads into the retail leased lines market in Guernsey, that entrants could price as competitively as they chose and that business end-users could take advantage of this choice through appropriately structured competitive procurement processes. In the GCRA's view, a correctly calibrated retail-minus control, augmented by a suite of flanking measures, could ensure that the SMP operator was not in a position to sustain excessive pricing in the regulated market. For all of these reasons, the GCRA proposed that a retail-minus approach was the most appropriate and proportionate means of meeting its objectives.

# 3. Responses to the Consultation and Draft Decision

## 3.1 Introduction

CICRA received a total of seven responses to its simultaneous consultations in Guernsey and Jersey on wholesale leased lines, from Sure; Jersey Telecom; Airtel; Nitel; ACS Telecommunications Consultants; Digital Jersey and C Burton.

Of these, three were provided on a pan Channel Island basis or specifically addressed both Guernsey and Jersey issues. The response from C Burton was Guernsey specific while the responses from Nitel, Digital Jersey and ACS consulting were focussed on Jersey. However, a number of issues raised in the Jersey specific responses are relevant to the broader pan CI issues and where appropriate these have been drawn on in the comments below.

CICRA would like to thank each of the respondents for their input to this process. Copies of the responses are published on CICRA's website, www.cicra.gg, apart from those sections highlighted by the respondents as confidential.

As it stated in the Draft Decision, the GCRA's overall strategy is to put in place mechanisms that allow OLOs to compete effectively in the market, as effective competition will best deliver benefits for end-users. As well as further specifying the price control, the Draft Decision also set out proposals for a number of supporting remedies to strengthen the proposed retail-minus price control. In particular, the GCRA proposed that remedies in the areas of non-discrimination and accounting separation as well as measures to strengthen compliance should be adopted with the aim of providing greater benefits for end-users.

**Proposal: a retail-minus price control will be imposed, strengthened by the implementation of supporting remedies.**

| **Q1: do you agree with the GCRA's proposal to implement a retail-minus price control, strengthened by supporting remedies? If not, what alternatives do you suggest?** |
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***Responses***

Sure, JT, ACS, and Nitel agreed that a retail-minus control was the most appropriate option. Sure raised a number of points regarding the use of supporting remedies in Jersey, and these are discussed in the relevant section of the Jersey response to consultation.

Airtel did not agree with the GCRA's approach. Airtel stated that it would prefer to see a "cost plus" approach to leased line pricing because in its view this would encourage increased competition in the leased line market.

C Burton expressed a view that a cost modelling exercise should be undertaken to understand the implications and facilitate the introduction of a pure wholesale connectivity suite of products.

***GCRA analysis***

The GCRA notes that the submission by C Burton proposes an alternative approach to regulating the market for wholesale leased lines. The GCRA has addressed specific points made below where relevant, but does not intend to reopen a discussion about issues which are outside the scope of this review of the price control to be applied to wholesale on-island leased lines. In terms of a cost modelling exercise, the GCRA's view is that such an approach would take some time to implement, and the ultimate benefit for retail customers is not guaranteed, and that the approach proposed by the GCRA was likely to deliver benefits in the market in a shorter timeframe and in a more proportionate manner which recognised the need to balance lower prices for end users with investment in new products and services.

It is not entirely clear how or why a cost plus approach advocated by Airtel would encourage competition in the market, in many ways it may be less favourable to competitors and offer fewer incentives to compete because it would not guarantee a specific margin or headroom in the retail market in which they can operate. Airtel's comments may be based on an assumption that cost plus pricing would result in lower pricing but there is no evidence to support this view.

The GCRA has emphasised the fairness of the principle that prices charged to end-users should be related to the costs of supplying products and services. In the GCRA's view, the proposals set out in the Decision for a retail-minus control with supporting obligations addresses this principle through establishing clear rules about how wholesale on-island leased lines are to be supplied, and how Sure is to demonstrate that they are supplied in a way which complies with all of its obligations. The proposals set out by the GCRA include a requirement for Sure to provide a regular compliance statement which will facilitate increased transparency around pricing and costs of leased lines, and in the GCRA's view, this option meets the GCRA objectives in a way which is appropriate and proportionate.

***GCRA conclusion***

The GCRA has decided to to implement a retail-minus price control on the wholesale market for on-island leased lines, strengthened by supporting remedies.

## 3.2 Options for restructuring the control

The GCRA considered a number of options regarding how such a control could be structured, and invited respondents to comment on each element in turn.

## 3.3 Should the control be applied ex ante or ex post?

***The GCRA's Consultation and Draft Decision proposals and questions***

The Draft Decision considered whether the control should be set on an *ex ante* or *ex post* basis. An *ex ante* control sets in advance the margin that should exist between retail and wholesale provision of leased line services. An *ex post* approach would instead involve the GCRA checking whether or not a sufficient margin existed between the price of retail and wholesale leased lines in response to a complaint.

In general, an *ex post* approach would be geared towards examinations of possible abuses of dominance which have already occurred, while an *ex ante* approach would be set with the aim of preventing an abuse of dominance from taking place. At present, although the price control in Guernsey is theoretically set as an *ex ante* control, it operates in practice as an *ex post* control, in that compliance is assessed on the basis of a complaint of specific practices. The conclusions reached in the market review indicate that the use of an *ex ante* approach is more appropriate, and the GCRA proposed to implement fully an *ex ante* approach, with the use of supporting remedies as discussed in the section below.

***Q2: do you agree that the control should be set ex ante? If not, why not?***

***Responses***

Of the respondents who commented on this question, all agreed that the control should be imposed on an *ex ante* basis.

***GCRA analysis***

The GCRA maintains that it is essential that the control is applied on an *ex ante* basis, such that it will apply in advance to the provision by Sure of all wholesale on-island leased lines in Guernsey.

*GCRA conclusion*

| The price control will be imposed on an *ex ante* basis. |
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### 3.4 Should the control apply to all wholesale leased lines?

***The GCRA's Consultation and Draft Decision proposals and questions***

The GCRA defined a market for wholesale on-island leased lines which included all capacities of leased lines. However, a retail-minus control in the wholesale on-island leased lines market could be set either on all capacities of wholesale circuits or on a sub-set of them. This could mean that some capacities of wholesale leased lines would potentially be made exempt from the proposed price control.

Placing some capacities outside the control might be justified on the grounds that there is little or no demand for the capacities in question, or that there is some difference in the conditions of competition which, although not sufficient to warrant the definition of a separate market, may indicate that a different regulatory approach is justified. Set against this, however, is the desirability to transition end-users from lower capacity to higher capacity leased lines. This could mean that capacities for which demand is currently low could be in greater demand over the short-to-medium term and so competing operators using wholesale inputs would need access to these capacities at regulated rates as they currently do for other capacity leased lines.

The GCRA's preliminary view in the Draft Decision was that there was insufficient justification for excluding particular types of line from the price control at this time, and that the direction of market development suggested that operators should be encouraged to support end-users who wished to move towards higher capacity connectivity.

| **Q3: do you agree that the control should apply to all wholesale on-island leased lines? If not what alternatives do you suggest?** |
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***Responses***

Sure, JT, Nitel, ACS, and Airtel agreed that all wholesale on-island leased lines should be included in the control.

C Burton expressed a view that a new approach to modelling wholesale services should be facilitated and encouraged by CICRA.

***GCRA analysis***

The GCRA maintains that there is no reason to exclude any wholesale on-island leased lines from the control, and that it should apply to all wholesale on-island leased lines.

***GCRA conclusion***

| The price control will apply to all wholesale on-island leased lines. |
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### 3.5 Should the control be applied on a product-by-product basis or to a set of products?

***The GCRA's Consultation and Draft Decision proposals and questions***

A product-by-product approach means that the SMP operator must ensure that every type of wholesale leased line offered for sale complies with the retail-minus formulation, while a portfolio approach means that compliance must be at the level of a group of products. The decision about whether to apply the control on a product-by-product basis or by using some form of grouping or portfolio approach balances the wish to give the SMP operator some pricing flexibility against the need to ensure that there is no scope for margin squeeze within a portfolio.

The GCRA stated in the Draft Decision that it had considered whether the costs associated with different types of wholesale and retail leased lines vary to the extent that a portfolio approach would be problematic. The GCRA also stated that it had considered the extent to which it would be difficult for operators to demonstrate compliance if the level of the control were too highly aggregated.

The GCRA's preliminary view in the Draft Decision was that a product-by-product approach offered the highest degree of certainty regarding the implementation of the control.

| **Q4: do you agree that the control should apply to each wholesale on-island leased line? If not, what alternatives do you suggest?** |
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***Responses***

Sure, JT, ACS, Airtel, and Nitel agreed that the control should apply to each wholesale on-island leased line.

C Burton proposed that a different approach was required, and reiterated the need for this.

***GCRA analysis***

The GCRA maintains that the control should apply to each wholesale on-island leased line, as this offers the greatest reassurance of transparency in the implementation of the control, and in particular the avoidance of margin squeeze.

***GCRA conclusion***

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| The price control will apply to each wholesale on-island leased line. |

**3.6 Matching wholesale and retail products**

***The GCRA's Consultation and Draft Decision proposals and questions***

The GCRA put forward the preliminary view that every type of retail leased line offered for sale should have a wholesale equivalent which is priced in a way that complies with the market-level control. This approach would be justified in terms of Sure's obligation that it must not unduly discriminate between OLOs and between OLOs and its own downstream operation. Ensuring that there is a wholesale variant for each and every retail offering will enable access-based competitors to replicate the SMP operator's retail leased line product offerings using appropriate wholesale inputs.

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| **Q5: do you agree that every retail on-island leased line product offered by Sure must have a wholesale equivalent? If not, what alternatives do you suggest?** |

***Responses***

Sure proposed that the GCRA's proposal could unnecessarily stifle innovation, and that instead, the focus should be on the ability of OLOs to fairly replicate any retail services provided by an incumbent, so that where an incumbent offers a retail service it should be based on standard underlying wholesale services.

JT, ACS, Airtel, Nitel agreed that all retail on-island leased lines offered by Sure should have a wholesale equivalent.

C Burton proposed that the GCRA's approach was unfair, particularly in Guernsey, where Sure should not be obliged to offer wholesale equivalents of its retail products.

***GCRA analysis***

In the GCRA's view, it is important to retain the principle that undue discrimination should not occur between how the SMP operator treats OLOs on the one hand and how it treats its downstream arm on the other. The maintenance of this obligation should not stifle innovation, as both the SMP operator and OLOs are not prevented from bringing different retail products to market, but it will prevent market foreclosure by the dominant provider and so it should be retained.

***GCRA conclusion***

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| Every retail on-island leased line product offered by Sure must have a wholesale equivalent. |

### 3.7 How to treat discounts/temporary promotions

***The GCRA's Consultation and Draft Decision proposals and questions***

In terms of setting the wholesale control, an issue arises as to whether or not any discounts or temporary promotions made available by Sure at a retail level should also be made available at the wholesale level. So, for example, if retail customers are offered preferential terms for purchasing an extended term contract or can avail of time-limited retail promotions for particular types of leased lines, the issue is whether or not this should be mirrored at the wholesale level.

The GCRA explained in the Draft Decision that although it might seem to make intuitive sense to frame the control so that retail discounts and promotions are mirrored at the wholesale level, a key question was whether or not wholesale customers would avail of or attribute the same value to the kind of discounts and promotions that were made available at the retail level. If not and the control were framed in a way that obliged the SMP operator to mirror such retail discounts in its wholesale pricing, then there would be a danger that wholesale customers might not enjoy the same level of retail-minus discounts in the prices they would have to pay for wholesale leased lines (given that the SMP operator would be entitled to include such discounts when demonstrating compliance with the control).

Arising from this concern, the GCRA's preliminary view was that retail discounts and promotions should not have to be made available at the wholesale level and it sought feedback, in particular from purchasers of wholesale leased lines, on the matter.

**Q6: should all retail price discounts and temporary promotions be mirrored in wholesale level pricing? If not, what alternatives do you suggest?**

***Responses***

Sure proposed that retail price discounts and temporary promotions should not be mirrored at the wholesale level. In Sure's view, term savings are only evident at the retail level. For example, where a retail customer signs up for a three-year deal the retailer has saved itself the cost of marketing/client relationship as the end of the year approaches, as the customer is already committed to a second/third 12-month term. However, at the wholesale level, the incumbent operator doesn't incur any similar marketing/client relationship costs, as none of its services are marketed – they're simply made available to retailers – so there are no equivalent costs to be saved at the wholesale level.

JT agreed that retail discounts and promotions should not have to be made available at the wholesale level.

ACS, Airtel, Nitel and C Burton disagreed. ACS indicated that it is difficult to determine the exact point of saving in a fully integrated incumbent telco. Airtel noted that an alternative cost-plus model would leave decisions about discounts in the hands of the operator, so fostering greater competition. Nitel suggested that discounts and promotions undermine the retail margin offered to OLOs. C Burton reiterated his/her view of the need for a more progressive approach.

***GCRA analysis***

The GCRA accepts the point made by Sure that costs saved from offering term discounts at the retail level reflect savings made at the retail level rather than the wholesale level of the operator.

In addressing concerns expressed by other respondents, the GCRA's view is that these concerns are to do with the implementation of the control rather than with the specific operation of discounts. The GCRA agrees with respondents that there is a need for increased transparency around the pricing and costing of leased lines, and the supporting measures which the GCRA is putting in place directly address this concern. The price control will oblige Sure to maintain a margin between its wholesale and retail prices, which will prevent margin squeeze on an ex ante basis – Sure will not be able to launch a new product or service without ensuring that it fulfils all of its regulatory obligations in advance of the launch. OLOs purchasing wholesale on-island leased lines may price at the retail level as they choose, and may offer any discounts as they see fit.

Operators will have to comply with the price control at an overall level (product by product) and the wholesale prices offered to other operators will reflect this at an aggregate level. For example, if an operator offers term discounts for its retail leased lines (eg, 10% discount for a 3 year period) then it wouldn't be required to also offer a 3 year, 10% reduced wholesale leased line, but the overall price of equivalent leased lines might be lower than otherwise, to reflect the discount averaged across all of those products, including the discounts. Some examples to demonstrate how the average retail price would be calculated to take into account discounts, promotions or other rebates are set out in Annex 3A.

Further, the GCRA notes that Condition 31 of Sure's licence states that:

*"All published prices, discount schemes and special offers of or introduced by the Licensee for Licensed Telecommunications Services shall be transparent and non-discriminatory; all discount schemes shall be cost-justified and all special offers shall be objectively justifiable".*

***GCRA conclusion***

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| Retail price discounts and temporary promotions offered by Sure do not need to be mirrored in its retail-minus wholesale level pricing. |

## 3.8 What form should the control take?

***The GCRA's Consultation and Draft Decision proposals and questions***

At a conceptual level, a retail-minus price control for a wholesale service involves setting the wholesale price by reference to the retail price, deducting those costs which an efficient wholesale SMP operator is able to avoid by supplying the service in question to another operator at the wholesale level as opposed to selling it directly to customers at the retail level. This means that efficient market entrants will be able to offer competitive products and services to their own retail customers.

As regards the specific way that the retail-minus amount should be expressed within the control, the GCRA stated in the Draft Decision that there were two broad options for doing this, i.e. by setting the minus as an absolute fixed monetary value or by setting the control as a fixed percentage of the retail price.

Given that leased line pricing would be unlikely to fluctuate significantly, the GCRA's preliminary conclusion in the Draft Decision was that it should proceed with a control that set the wholesale price as a fixed percentage of the retail price.

**Q7: do you agree that the control should be set as a fixed percentage? If not, why not?**

***Responses***

Sure, JT, ACS, and Airtel agreed that the control should be set as a fixed percentage.

Nitel disagreed and proposed an alternative model, where a series of retail-minus percentages would be offered based on the turnover of the OLO. C Burton disagreed due to his/her underlying disagreement with the overall retail-minus approach.

***GCRA analysis***

The GCRA has considered whether a number of different percentages should be offered. While understanding the rationale put forward by Nitel, the GCRA does not favour the introduction of additional wholesale discounts for small operators or reduced prices to favour market entrants over incumbents as a principle. In general it is not compatible with sound economic regulatory practice. Not only would it be difficult to implement in practice, but it sends misleading economic signals and runs a serious risk of encouraging inefficient entry into the market, or of supporting inefficient economic activity, to the overall detriment of customers in the long run.

The GCRA therefore maintains that the control should be a fixed percentage of the retail price.

***GCRA conclusion***

The control will be set as a fixed percentage of the retail price.

### 3.9 At what level should the value of the minus be set?

***The GCRA's Consultation and Draft Decision proposals and questions***

In considering the appropriate value of the minus, the GCRA explained in the Draft Decision that it must ensure it is not set too low, which would leave insufficient space for a market entrant to compete, and is not set too high, which could both reward inefficiencies in market entry, and fail to recognise Sure's costs in providing a wholesale service. The GCRA stated that it had taken into account its experience of price regulation both in Guernsey and in other jurisdictions, and had also taken into account typical margins that prevailed between retail and wholesale leased lines. The GCRA's preliminary proposal was that retail minus 20% offered a fair and reasonable margin in which OLOs could compete in the retail leased lines market.

**Q8: do you agree that retail minus 20% is an appropriate margin? If not, what alternatives do you suggest?**

***Responses***

Sure and JT agreed with the proposed margin.

C Burton and Airtel reiterated that they believe the control should be cost-plus rather than retail-minus.

Nitel expressed a view that a single rate is too restrictive, and does not recognise the variety and size of competitors in the market.

***GCRA analysis***

The GCRA notes that setting the value of the minus must take into account a number of objectives. The margin must be set high enough to allow space for market entrants to compete, but not so high that it rewards inefficient market entry. The margin must also recognise Sure's costs in providing a wholesale service. The GCRA notes that no respondent provided any evidence or rationale to justify a different margin.

***GCRA conclusion***

The price control will be set at retail minus 20%.

### 3.10 Should the control be set in a way that eliminates differential pricing?

***The GCRA's Consultation and Draft Decision proposals and questions***

In Guernsey, Sure's pricing of leased lines differs depending on whether or not the circuit from the customer's premises terminates within the same exchange area or a different exchange area than where it originates. The issue for the GCRA to consider is whether or not it should seek to use the formation of the revised price control on leased lines to limit or eliminate such differential pricing.

As it explained in the Draft Decision, the GCRA took the view that it would not be appropriate to use the price control remedy as a means to eliminate differential pricing in the provision of leased lines. The GCRA noted in the Draft Decision that Sure was not prohibited from eliminating such pricing of its own accord and that this would also be the case under the proposed new price control framework.

The GCRA also noted that its approach emphasised its support for investment in infrastructure and for a transition to Next Generation access and services, with technology developments likely to result in differential pricing being phased out by operators over the medium term. In light of this, the GCRA's preliminary view was that it would not deal further with the issue of differential pricing as part of this review.

**Q9: do you agree that it is not appropriate to use the price control mechanism to address differential pricing? If not, why not?**

***Responses***

Sure expressed a view that differential pricing was justified in Guernsey, because the same exchange/different exchange difference recognised additional equipment and longer line lengths, but not in Jersey, where, in Sure's opinion, the 300 metres differentiator is artificial. Sure stated that it was unlikely to remove differential pricing voluntarily, and expressed disappointment that CICRA was not seeking to remove differential pricing through the review.

JT agreed that it is not appropriate to use the price control mechanism to remove differential pricing.

Airtel put forward an opinion that the price control would help to control differential pricing because the cost of supply would be clear.

Nitel considers that differential pricing should be abolished.

***GCRA analysis***

The pricing of all wholesale leased line is subject to the "retail minus" price control so where there is differential pricing in retail products, this will have to be reflected in the equivalent wholesale price.

The GCRA reiterates its view that, as under the existing price control, Sure is free to eliminate differential pricing of leased lines under the new price control framework should it wish to do so. In light of this, and given that technology developments are likely to lead to the elimination of differential pricing over the medium-term, the GCRA maintains its position that the issue is one for the telecoms operators themselves to address. The GCRA would expect that the operators would respond to the demands of their customers, and would expect any differentiated pricing to fairly reflect differences in the cost of providing the service.

The GCRA retains the option to investigate the pricing and offer of products if it appears that the effect is to distort market or to abuse a position of dominance in the wholesale market to benefit its own retail operations. There is no evidence to suggest that this is the case at present.

***GCRA conclusion***

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| The issue of differential pricing of leased lines by Sure will not be addressed as part of the price control review. |

## 3.11 Summary of conclusions on the structure of the control

In relation to how the proposed retail-minus control should be structured, the GCRA has reached the following conclusions:

- The control should be set on an *ex ante* basis;
- the control should apply to all wholesale on-island leased lines;
- The control should be applied on a product-by-product basis;
- for each retail leased line product offering, a wholesale equivalent product must be offered at a price that complies with the proposed control;
- The control should be set at retail minus 20%;
- The control will not separately address differential pricing.

## 3.12 Time period over which control in place

***The GCRA's Consultation and Draft Decision proposals and questions***

In the Draft Decision, the GCRA put forward the view that the most appropriate approach would be to link the control to the market review process. This would mean that decisions about the control would be taken consistently with decisions about market definition and market power. The GCRA considered that this approach would also be appropriate in view of the fact that the rate of change in wholesale on-island leased lines products and services is likely to be quite limited.

**Q10: do you agree that the term of the price control should be aligned with the market review cycle? If not, what alternatives do you suggest?**

***Responses***

JT, C Burton, Airtel and ACS agreed that the term of the price control should be aligned with the market review cycle. Sure noted the proposal, but stated that there was no indication of the likely frequency of the market review cycle. In Sure's view, the rate of change in the market in Guernsey would warrant a further market review within the next 24-36 months. Sure asked for information on the process whereby a market review could be requested outside of whatever is deemed to be the 'normal' cycle.

***GCRA analysis***

The GCRA notes that none of the respondents were opposed to its proposal that the term of the price control should be aligned with the market review cycle. As regards Sure's point about when the next market review will be undertaken, the GCRA confirms that it will keep market developments under active review on an ongoing basis. The GCRA notes further that the reporting and monitoring requirements which are being put in place as part of this price control decision will enable closer analysis of market change. However, the GCRA would be open to consider reviewing the market in response to evidence of significant market change.

***GCRA conclusion***

The term of the price control will be aligned with the market review cycle.

### 3.13 Supporting remedies

***The GCRA's Consultation and Draft Decision proposals and questions***

In the Draft Decision, the GCRA stated that a number of supporting remedies would be required in order to ensure that the price control works effectively. The key remedies put forward by the GCRA in this context were:

- ***Non-discrimination:*** wholesale on-island leased lines must be made available to OLOs in a manner which does not discriminate between OLOs, and between OLOs and Sure's own downstream retail operation. In terms of the price control, any wholesale price terms which are available to Sure's downstream operation should also be made available to OLOs.

- ***Cost accounting/accounting separation:*** Sure will be required to produce separated accounting information for wholesale on-island leased lines, which will provide more focused data on this market, including the operator's rate of return. While the GCRA accepts that separated accounting information is not in itself an indicator of cost orientation, it does provide a headline indication of any unreasonable profit in a market where the operator has been found with SMP.
- ***Transparency:*** Sure will be required to submit a regular statement formally confirming its compliance with the wholesale price control. This compliance statement will need to include details of prices, number of lines sold, revenues earned and promotional offers made for all retail and wholesale leased lines, by bandwidth.

The GCRA proposed in the Draft Decision that this compliance statement would need to be furnished by Sure on a quarterly basis and, hence, that it will also need to demonstrate compliance with the control every quarter. It was proposed that the first quarterly compliance statement would be submitted by Sure in relation to Q3 2015 and that this statement will be submitted to the GCRA no later than Friday, 16th October 2015.

**Q11: do you agree with the GCRA's proposed use of supporting remedies? If not, why not?**

***Responses***

Sure agreed that it would provide the visibility required by the GCRA through a quarterly compliance statement.

ACS was supportive of the proposed approach. Airtel stated that the remedies were acceptable as far as they go. JT noted that CICRA is consulting separately on the separated accounting regime in the Channel Islands, and expressed a view that any proposed changes to the regime that relate to leased lines should be part of that process. JT suggested that the proposed frequency of reporting was overly burdensome, and suggested that six-monthly reporting was more appropriate particularly as the leased line market is fairly static. C Burton expressed a view that the approach proposed in his/her submission would require fewer supporting remedies and reporting.

***GCRA analysis***

The GCRA notes that there is no opposition from respondents to its proposal that a range of supporting remedies be put in place to ensure that the revised price control works effectively in practice. The GCRA notes the point made by JT in relation to the separate consultation process being undertaken by CIRCA in relation to the separated accounting regime in the Channel Islands. In response, the GCRA reiterates that its proposed use of separated accounting data for the wholesale on-island leased line market will enable it to check compliance with the revised price control and that Sure will be obliged to make the information available to it for this purpose.

The GCRA notes that the compliance statement which will be required from Sure will provide more granular and more up-to-date information than is currently available, and that this will be important for ensuring that the price control works effectively.

The GCRA has considered JT's point on the frequency of reporting. However, it has decided to maintain that reporting should be done initially on a quarterly basis in order to evaluate the functioning of the price control. On the basis of its evaluation of the initial process, the GCRA will consider whether reporting may be less frequent in subsequent years.

***GCRA conclusion***

| |
|---|
| Supporting remedies in the areas of non-discrimination, cost accounting, accounting/accounting separation and transparency should be put in place to ensure that the price control works effectively. |

**3.14 Other issues raised**

C Burton provided a perspective on an alternative wholesale model for connectivity, in particular hub and spoke Ethernet. In C Burton's view, the requirements for wholesale and retail connectivity are different and diverging, and this is not compatible with the current product set. According to C Burton, the hub and spoke proposal formed part of CICRA's Wholesale Access Project (CIWAP).

***GCRA comment***

The GCRA recognises that there are different views as to how the connectivity market may develop. The kinds of issues raised by C Burton have been considered and consulted on by the GCRA, both in the business connectivity market review, and in the context of the CIWAP. The GCRA notes that C Burton's response is outside the scope of this current consultation on the price control to be applied in the wholesale market for on-island leased lines, and does not propose to reopen earlier debates.

# 4. Final Decision

The GCRA's statutory powers are set out in Annex 1 of this response to consultation and draft decision.

The provisions of the consultation document and this Response to Consultation shall, where appropriate, be construed with this Decision. The analysis set out through the consultation process explains the reasoning behind the proposals, and indicates the effects the proposals are expected to have and gives reasons for making the proposal.

The price control shall be applied to Sure (Guernsey) Ltd in the wholesale market for on-island leased lines in Guernsey as follows:

- The control shall be set on an *ex ante* basis;
- the control shall apply to all wholesale on-island leased lines;
- The control shall be applied on a product-by-product basis;
- for each retail leased line product offering, a wholesale equivalent product must be offered at a price that complies with the proposed control;
- The control shall be set at retail minus 20%.

The term of the price control will be aligned with the market review cycle.

The price control will come into effect on 1 July 2015.

Sure will be required to submit a regular statement formally confirming its compliance with the wholesale price control. This compliance statement will need to include details of prices, number of lines sold, revenues earned and promotional offers made for all retail and wholesale leased lines, by bandwidth. The precise content of the compliance statement will be determined by the GCRA.

The GCRA recognises that there may potentially be some overlap in reporting between any proposals to revise regulatory accounts – a separate work stream within CICRA's existing work programme. So far as possible, CICRA would seek to ensure that any overlap is minimal and ensure the two approaches are consistent. However, it would not be appropriate to delay the implementation of formal monitoring of the WLL price control while waiting for the wider separated accounting project to come to fruition. It is worth noting in any case that compliance reporting for the price control will initially be required on a quarterly basis, with a view to moving to a six monthly basis in the future, while separated accounts would be prepared on an annual basis and would not be the appropriate vehicle to monitor and ensure compliance with this wholesale price control.

An indicative example is set out in Annex 3(B). This illustrates the information which would typically be required by the GCRA to monitor compliance. Sample calculations are set out in part 3(C) to show how compliance would be checked product by product.

Prices remain subject to the normal requirements of the Telecoms Law; the Competition (Guernsey) Ordinance, 2012 and Sure's telecommunications licence, in ensuring that charges are cost-justified where required and avoid discrimination. This safeguards, for example, against Sure (Guernsey) Limited offering services to its own retail arm on favourable terms or setting wholesale prices which unfairly prevent competitors from entering the market or competing against Sure.

## Annex 1: Legal Background and licensing framework

In its Decision Notice of February 2008[3], the Office of Utility Regulation (OUR) in Guernsey considered that Sure[4] was dominant in the wholesale fixed line telecommunications market (including, inter alia, on- and off-island leased lines) and the retail fixed line telecommunications market. The OUR identified two baskets of leased line services which were subject to price control regulation. These were:

- Basket 4: on-island wholesale leased lines, RPI-RPI, and
- Basket 5: off-island retail leased lines, RPI-RPI.

In addition, wholesale off-island leased lines were subject to a price cap set at retail minus 15%.

Following a review of Sure's wholesale business, the OUR published a set of Decisions[5] addressing Sure's conduct in the leased line markets. The Decisions addressed Sure's processes for the ordering and delivery of wholesale leased lines; a requirement to publish Key Performance Indicators (KPIs); penalties for failure to meet targets; changes to wholesale and retail upgrades and price changes; and establishment of a separate wholesale business structure.

The price control on Baskets 4 and 5, and the retail minus price cap on wholesale off-island leased lines were rolled over from 1 April 2011 to 31 March 2012[6]. In 2012, a review of the price control maintained a freeze on prices in Baskets 4 and 5, and maintained the retail minus control on wholesale off-island leased lines[7]. The review of the price control resulting in a Decision in March 2013 maintained an aggregate price freeze on Baskets 4 and 5, but allowed Sure to rebalance charges within the baskets. It was also decided that the price control period should end on 31 December 2013. The price control on Baskets 4 and 5 was extended in December 2013[8], pending either any changes imposed on the foot of this market review of business connectivity, or in December 2014, whichever is the sooner.

[3] *Price Control for Cable & Wireless Guernsey, Decision Notice*, Document No OUR 08/07 February 2008.
[4] Then Cable & Wireless Guernsey.
[5] *Review of C&W Guernsey's Wholesale Business, Decision Document,* Document No: OUR 08/16, October 2008.
[6] *Cable & Wireless Guernsey Price Control, Final Decision*, Document No. OUR 11/02, January 2011.
[7] *Cable & Wireless Guernsey price control for 2012-2013, Final Decision*, Document No. CICRA 12/24, March 2012.
[8] *Sure (Guernsey) Ltd., price control 2014 for exchange lines, calls and on-island (wholesale) and off-island (retail) leased lines, Draft Decision*, Document No. CICRA 13/52, December 2013, *Final Decision* Document No. CICRA 14/08, February 2014.

The GCRA published its Final Decision on the Business Connectivity Market Review (BCMR) in Guernsey on 1 October 2014[9]. The BCMR concluded that Sure continues to hold Significant Market Power (SMP) in the market for on-island wholesale leased lines in Guernsey, but not in the market for off-island wholesale leased lines, and not in the market for retail leased lines. SMP regulation was therefore withdrawn from the wholesale market for off-island leased lines, and the retail market.

The GCRA consulted on an extension to the price control on wholesale on-island leased lines, pending the outcome of the review of the price control. The Final Decision[10] published in December 2014 extended the previous control, and continued the price freeze on the overall basket of wholesale on-island leased lines.

The GCRA notes that the form and implementation of the price control are addressed in Condition 31 of Sure's licence, as follows:

" 31.1 Where the Licensee intends to introduce:

*(a) new prices for any Licensed Telecommunications Services, or prices for new Licensed Telecommunications Services to be introduced by the Licensee;*

*(b) any discounts to published prices for Licensed Telecommunications Services within a Relevant Market in which the Licensee has been found to be dominant or for any Subscribers to whom additional services or goods are provided by the Licensee or any of its Associated Companies; or*

*(c) special offers to all or any of its customers for particular categories of Licensed Telecommunications Services where those Licensed Telecommunications Services have been found to be within a Relevant Market in which the Licensee has been found to be dominant, it shall publish the same at least twenty one (21) days prior to their coming into effect or otherwise as required by law, and provide full details of the same to the Director General.*

31.2 The Director General may determine the maximum level of charges the Licensee may apply for Licensed Telecommunications Services within a Relevant Market in which the Licensee has been found to be dominant. A determination may;

[9] Document No CICRA 14/49

[10] Sure (Guernsey) Ltd., Price Control, wholesale leased lines, Document no CICRA 14/65, December 2014

*(a) provide for the overall limit to apply to such Licensed Telecommunications Services or categories of Licensed Telecommunications Services or any combination of Licensed Telecommunications Services;*

*(b) restrict increases in any such charges or to require reductions in them whether by reference to any formula or otherwise; or*

*(c) provide for different limits to apply in relation to different periods of time falling within the periods to which any determination applies.*

31.3 All published prices, discount schemes and special offers of or introduced by the Licensee for Licensed Telecommunications Services shall be transparent and non-discriminatory; all discount schemes shall be cost-justified and all special offers shall be objectively justifiable.

31.4 If the Director General, after consulting the Licensee and such other persons as she may determine, is satisfied that any published price, discount scheme or special offer is in breach the Regulation Law, Telecommunications Law or this Licence, the Director General may, by issuing a direction, require the Licensee to bring the relevant prices, discount schemes or special offers into conformity with the Laws and/or the requirements of this Licence."

## Annex 2: Glossary

***4G:*** Fourth-generation mobile telecommunications technology, which enables the delivery of high-speed broadband services over mobile networks. The '4G' standard encompasses the Long Term Evolution (LTE) technology, which is the main 4G technology being deployed worldwide.

***Alternative Interface (AI):*** new types of technologies used for delivering leased lines services, for example *Ethernet* (see below), which contrast with legacy *TI* technologies (see below).

***Asymmetric Digital Subscriber Line (ADSL):*** a broadband technology that enables high-speed data transmission over legacy copper local access telephony networks, using a high data rate in one direction and a lower data rate in the other.

***Bandwidth:*** The physical characteristic of a telecoms system that indicates the speed at which information can be transferred, which in digital systems is measured in bits per second (bps).

***Cloud computing:*** the use of a network of remote servers connected via the internet that store, manage and process data that would otherwise be handled on a local server or computer.

***Dark fibre:*** unused or 'unlit' optical fibre, i.e. fibre which has been deployed within a communication network but which is not connected to active electronic equipment used to facilitate data transmission.

***Direct internet access (DIA):*** a dedicated connection to the internet provided directly from the customer's site over a permanent link (also known as *IP feed* – see below).

***Ethernet:*** a technology used for data transmission. Originally deployed for use in a *LAN* (see below) environment, the technology has also increasingly been used to support *WAN* (see below) connectivity, with Ethernet being used in this instance as a leased line technology.

***Ex ante:*** the application of regulation before an abuse of power has necessarily occurred. The reasoning behind its application is that finding that an operator has SMP means that the operator is likely to have the incentive and motivation to behave in a way which exploits its market power to the detriment of competitors and ultimately to consumers. *Ex ante* regulation can be contrasted with *ex post* regulation, which investigates an incident which has already happened.

***Ex post***: the use of regulation following a complaint or abuse of market position by an operator. In contrast to *ex ante* regulation (see above).

***Internet Protocol:*** the communications protocol used for transmitting a data packet between a source and a destination on data networks, including the internet (also known as *Direct internet access* – see above).

***Internet Protocol (IP) feed:*** a dedicated connection to the internet provided directly from the customer's site over a permanent link.

***Leased line:*** A permanently connected communications link between two premises dedicated to a customer's exclusive use (see also *Private circuit* below).

***Local Area Network (LAN):*** a network that connects a number of devices that are relatively close together, for example within the same office or building, which enables intercommunication amongst users and access to private voice, email, internet and intranet services and applications.

***Modified Greenfield approach:*** a regulatory approach that works on the assumption that there is no *ex ante* (see above) regulation in the market in question, but takes account of the fact that upstream *ex ante* regulation is in place.

***Multi-protocol label switching (MPLS):*** a mechanism for directing data within and across networks from one network node to the next, with data packets being given a specific forwarding label at the point at which they enter the network, thus enabling more efficient routing.

***Plesiochronous Digital Hierarchy (PDH)***: a technical data transmission standard that enables transmission of data that generally runs at a similar rate to have a slight variation in actual data speed compared to the nominal rate. In recent years, PDH transmission has largely been replaced within telecoms networks by *SDH*, (see below).

***Private circuit:*** an alternative term for a *Leased line* (see above).

***Retail Price Index (RPI):*** a measure of inflation, published monthly by the Office for National Statistics in the UK.

***Small but Significant Non-transitory Increase in Price (SSNIP):*** a theoretical price increase that forms part of the 'hypothetical monopolist' test used in market definition analysis. The price increase in question is usually considered to be in the range of 5 to 10 per cent.

***Synchronous Digital Hierarchy (SDH):*** a technical data transmission standard for the transmission, which has largely replaced traditional PDH (see above) transmission.

SDH is an international standard that enables high-bandwidth synchronous data transmission.

***Time Division Multiplex (TDM):*** a method of putting multiple data streams in a single signal by separating the signal into many segments, each having a very short duration. Each individual data stream is then reassembled at the receiving end based on the timing.

***Traditional Interface (TI):*** legacy technologies used for delivering leased lines services, of which the main one would be *TDM* (see above).

***Virtual Private Network (VPN):*** a private network where connectivity is extended by making use of the internet over which a virtual point-to-point connection is established, with various protocols being used to ensure data security over the public element of the network.

***Wave Division Multiplex (WDM):*** a transmission technology that enables multiple wavelengths of light to share the same fibre optic pair.

***Wide Area Network (WAN):*** a network connecting devices located in geographically dispersed locations, either in the same national area or across national boundaries.

# Annex 3: Calculating wholesale prices and compliance

**(A) Taking account of discounted retail prices in calculating wholesale prices**

There is a need to ensure that under the retail minus price control decision implemented in this document, discounts schemes, rebates and special offers which apply at the retail level are properly reflected in the calculation of the wholesale price. The telecoms operator is not required to directly mirror its retail discount schemes or offers at a wholesale level, but the price control ensures that, on aggregate, any discounts and promotions offered to retail customers will have an impact in reducing the overall wholesale prices for all customers.

The simple calculations below illustrate how typical retail discounts would be taken into account in the wholesale price.

**Example 1 – no retail discounts**

A telecoms operator which has SMP sells 10 leased lines to retail customers at a price of £100 per month over the period.

Under the [retail – 20%] price control, its wholesale price must be at least 20% below the retail level, ie, £80 per month or less.

**Example 2 – with retail discounts**

If the same operator sold the same 10 leased lines, nominally priced at £100 per month, but offered a 20% discount for signing up to longer term contracts, taken up by half its retail customers (giving 5 at £100/month and 5 at £80/month). The actual (weighted average) retail price given by the total income divided by the number of products would be £90 per month

The price control applied to this would require the wholesale price to be £72 pcm or less to achieve the discount of at least 20% required by the retail minus 20% price control.

**(B) CICRA monitoring of compliance with price control**

**Leased lines revenue and pricing – example information required**

| Leased line | RETAIL PRODUCT | | | WHOLESALE EQUIVALENT | | |
|---|---|---|---|---|---|---|
| Product | No. | PRICE | Revenue, £ Jul - Sep | No. | PRICE | Revenue, £ Jul - Sep |
| A | | | | | | |
| B | | | | | | |
| C | | | | | | |
| D | | | | | | |
| | | | | | | |

Revenue is revenue net of all discounts, rebates and refunds or other incentives provided to the purchaser.

Price is the standard price without discounts. If the price has changed during the period this should be clearly indicated in a covering note.

The operator should clearly indicate what discount or rebate schemes are in operation during the period.

Agency fees or bonuses provided to third parties which negotiate or procure services from the wholesale operator should also be clearly disclosed and treated in the same way as any other promotion or discounts against the retail price.

**(C ) Examples of price control compliance calculations**

**Reported information:**

| Type of Leased line | RETAIL PRODUCT | | WHOLESALE EQUIVALENT | |
|---|---|---|---|---|
| Product | No. | Revenue, £<br>1 Jul - 30 Sep | No. | Revenue, £<br>1 Jul 30 Sep |
| A | 80 | £45,000 | 20 | £9,000 |
| B | 20 | £37,500 | 5 | £6,000 |
| C | 10 | £75,000 | 5 | £33,000 |
| | | | | |
| | | | | |

**<u>For product A:</u>**

Average retail price for product A = pro rata revenue / no. of leased lines

= {£45,000 / 3months } / 80 = **£187.50 pcm (per calendar month)**

**CHECK: [Retail price – 20%] = £ 150 pcm**

Actual wholesale price (pro rata average) = (£9,000/3m) / 20 = £150 pcm

The actual wholesale price is equal to or less than the retail price minus 20% required by the price cap, therefore **it complies.**

**<u>For product B:</u>**

Average retail price for product B = ( £37500 / 3) / 20 = **£625 pcm**

**CHECK: [Retail price – 20%] = £ 500 pcm**

Actual wholesale price = £6,000 / 5 = **£400 pcm**

Wholesale price is below the retail – 20% price control, therefore **complies.**

**<u>For product C:</u>**

Average retail price for product C = ( £75,000 / 3 ) / 10 = **£2,500 pcm**

**CHECK: [Retail price – 20%] = £ 2,000 pcm**

Actual wholesale price = (£33,000/3) / 5 = **£2,200 pcm**

In this case, the wholesale price is greater than the retail minus price control of £2,000 pcm and therefore **does not comply with the price control.**