Office of Utility Regulation

C&WG Reference Offer and Interconnection Rates

Final Decision

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1. Introduction

One of the roles of the Office of Utility Regulation ("OUR") is to review and assess the interconnection and access charges included by C&W Guernsey Ltd ("C&WG") in its Reference Offer ("RO"), in order to ensure that they are cost oriented. The provision of interconnection and access services at reasonable and non-discriminatory rates is critical to the development of a well functioning, competitive telecommunications market. It is important that prices for interconnection and access services are set at cost in order to:

- support the development of effective competition;
- provide efficient 'build or buy' signals to new entrants; and
- enable the provision of competing services in retail telecommunications markets.

The charges which are currently included in C&WG's RO were set in March 2005.[1] Given the elapsed time since these charges were set and the developments in the market since this date, the OUR indicated, in October 2008, that it would commence a review of these charges. This review has considered whether the prevailing structure and level of charges remains appropriate and, where necessary, has developed a revised set of rates. As a starting point for this review, C&WG submitted to the OUR in February 2009 a proposed set of RO rates which it considered met the requirements for cost orientation.

In June 2009 the OUR published a consultation document on C&WG proposed interconnection and access charges going forward.[2] This consultation dealt mainly with the methodology and data used by C&WG to calculate interconnection and access charges, and proposed that revised rates should be based on C&WG's regulatory accounts for the 2008/09 financial year, which were due to be submitted by C&WG to the OUR by the end of October 2009.

The Director General of the OUR ("DG") received three responses to the consultation, namely from Guernsey Airtel Ltd ("Airtel"), Wave Telecom Ltd ("Wave") and C&W Guernsey Ltd ("C&WG). Two main issues emerged out of the responses, namely how and whether charges should be differentiated by time of day (i.e., the time of day gradient), and how interconnection link services should be charged for.

In October 2009, the OUR published its draft decision on these and other matters arising from the consultation process. Again, the DG received responses to the draft decision from Airtel, Wave and C&WG.[3] In January 2010, C&WG submitted to the OUR a revised set of interconnection rates, based on its 2008/09 regulatory accounts.

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[1] See OUR 05/09 (March 2005); http://www.regutil.gg/docs/OUR0509.pdf

[2] C&WG Reference Offer and Interconnection Rates, Consultation Document, OUR 09/08, June 2009, available at the OUR website.

[3] Non-confidential responses to the consultation and draft decision are available on the OUR's website (www.regutil.gg) and for inspection at the OUR's offices during normal working hours.

This document now responds to the comments received by the DG on the draft decision and sets out the OUR's final decision on C&WG's reference offer and interconnection rates. In publishing this decision document, the DG would like to acknowledge the high level of co-operation provided by all stakeholders in this matter. The rates now being determined by the DG will take effect from 1st April 2010.

2. Structure of the Decision

2.1 Structure of the Final Decision document

This consultation is structured as follow:

Chapter 3: sets out the legal framework and provides the regulatory background to the DG's review of the RO and interconnection rates;

Chapter 4: summarises the key points made by respondents to the Draft Decision; and

Chapter 5: sets out the DG's Final Decision, including revised RO and interconnection rates.

In accordance with the OUR's policy on consultation set out in Document OUR 05/28 – "Regulation in Guernsey; Revised Consultation Procedures Information Paper" – all non-confidential responses to the Draft Decision have been published on the OUR's website (www.regutil.gg) and are available for inspection at the OUR's office during normal working hours.

3. Legal Background & Regulatory Framework

3.1 Legal Background

Section 10 of the Telecommunications (Bailiwick of Guernsey) Law, 2001 ("the Telecoms Law") sets out the DG's powers with regard to interconnection and access and describes the requirements that the DG may impose on *inter alia* any licensee whom he determines has a dominant position in a relevant market. The DG has determined (Documents OUR 01/14 and 08/07), that C&WG has a dominant position both in the fixed telecommunications network and services market and in the mobile telecommunications network and services market. The OUR further informed C&WG that the provision of section 10(2) of the Telecoms Law would apply to it, thus requiring it in due course to;

(a) make its procedures for the provision of interconnection and access publicly available on a non-discriminatory basis in a manner that is to the reasonable satisfaction of the DG;

(b) offer a standard interconnection and access agreement (referred to as the "Reference Offer") which is available under non-discriminatory terms, conditions and charges, and on a non-discriminatory basis, no less favourable than that offered to -
   (i) any of C&WG's own services; or
   (ii) any associated company of C&WG's or services of such a company;

(c) provide interconnection or access on terms, conditions and charges that are transparent and cost-oriented having regard to the need to promote efficiency and sustainable competition and maximise consumer benefits;

(d) provide interconnection or access at any technically feasible point in its telecommunications network; and

(e) provide interconnection or access in a manner that is sufficiently unbundled so that the person requesting interconnection or access does not pay for telecommunications network components or telecommunications services that he does not require.

The legal responsibility is on C&WG to ensure that it provides such information as is necessary to fully demonstrate that any proposed charges for its interconnection and access services comply with its obligation under the Telecoms Law.

In addition, the Telecoms Law makes provision for the DG to direct changes to the standard interconnection and access offering and to require C&WG to justify its costs or charges for the provision of interconnection and access services.

3.2 Regulatory framework

Apart from having to comply with the Telecoms Law, C&WG also has to comply with the Licence conditions which the DG issued in 2001 and Directions which the DG has issued since.

The DG granted a 'Fixed Telecommunications Licence'[4] to C&WG "to establish, operate and maintain the Licensed Telecommunications Network". Part IV of this Licence includes a number of licence conditions applicable to dominant operators. As set out earlier, the DG has determined that C&WG has a dominant position both in the fixed telecommunications network and services market and in the mobile telecommunications network and services market.

The Licence also contains a section on information provision. Furthermore, in May 2005, the OUR published an information note on C&WG Interconnection and Access Charges.[5] This provides detailed guidance to C&WG on the minimum level of information which it should provide when submitting any proposed charges for interconnection and access services, in order to ensure its compliance with its obligations under the Telecommunications (Bailiwick of Guernsey) Law, 2001 and its licence. Publication of this detailed guidance followed a review of the previous RO submission made by C&WG in November 2003[6].

4 OUR 01/18, available at http://www.regutil.gg/docs/our0118.pdf
5 OUR 05/11, available at http://www.regutil.gg/docs/our0511.pdf
6 The details of this review are set out in OUR 05/09, available at http://www.regutil.gg/docs/OUR0509.pdf

4. Responses to the Draft Decision

This chapter summarises the main issues raised by the respondents to the Draft Decision. As such, it is not an exhaustive review of the responses received by the OUR to that document. The full responses can be found on the OUR website.

As with the responses to the consultation, the two main issues which emerged from the responses were:

1. The Time of Day ("TOD") gradient which should be applied to the interconnection charges; and
2. The charging for interconnection link services, including both the charge for new links and the on-going rental charges for existing links.

One respondent also raised the level of the proposed interconnection charges (based on C&WG's 2007/08 costing data), compared to the existing charge levels.

In many cases, the responses to the Draft Decision build on the responses made by licensees to the June 2009 consultation. In this section we do not, however, summarise those responses again.

4.1 The Time of Day Gradient

A time of day gradient converts the standard cost per minute into a peak or off-peak price per minute. Therefore, different tariffs are charged according to whether the call is carried in the peak or off-peak period. These gradients have typically served two purposes.

Firstly, a time of day gradient can support network traffic management. At times of relatively high demand for the network, operators will be charged the higher peak wholesale price, which will flow through to their retail prices and therefore flatten demand. Conversely, at times of relatively low demand for the network, operators will be charged the lower off-peak wholesale price, which will flow through to their retail prices and stimulate demand. Therefore, this pricing structure should encourage smoother network usage patterns. Network dimensioning is driven by demand in the peak hour. Therefore, if a time of day gradient reduces traffic in the peak hour it can serve to reduce the network capacity that is required and hence the costs of the network.

Secondly, given the nature of demand for telecommunications services, a time of day gradient may also act as a proxy for Ramsey pricing, whereby common costs are recovered relatively more from consumers with a higher willingness to pay. This is because most business customers (who may have a higher willingness to pay for communications services than residential customers) will make calls in the (more expensive) peak period, whilst residential customers will call primarily in (cheaper) off-peak periods.

The approach taken by C&WG to calculate the time of day gradients in its initial proposed rates followed broadly the methodology devised by BT in the UK. The gradient is determined using the retail prices of those services which are dependent on the wholesale service under consideration. Using the weighted average retail price per minute at peak and off-peak times, a peak gradient (the ratio between the peak and average retail price) and an off-peak gradient (the ratio between the off-peak and average retail price) are determined. In addition, any call types (such as premium rate services and fixed to mobile calls) where the retail price charged is dominated by termination charges from another network are excluded. This is because the pattern of demand for these call types cannot reasonably be influenced by the originating operator (C&WG in this case).

Draft Decision

In responses to the June 2009 consultation both OLOs argued that the TOD gradient on interconnection rates should be abolished and replaced with a flat rate. As set out in the Draft Decision, OLO's advanced a number of reasons for using flat rate charges, namely that:

- It would be simpler for OLOs as it would make interconnect invoice reconciliation easier;
- It would allow operators to introduce simpler pricing structures for consumers;
- It would reduce costs for OLOs and ultimately consumers (lower billing costs);
- There are in practice no capacity constraints on C&WG's network which require usage to be smoothed and furthermore, against the background of reducing fixed traffic volumes (and the transition to NGN) it is unlikely that capacity issues will occur in the near future; and
- It would be consistent with the structure of mobile termination rates in the Bailiwick (a flat rate MTR was adopted in April 2009).

In contrast, C&WG argued that adoption of a flat rate would likely result in network inefficiencies as it would re-introduce the potential for the network to become overloaded at peak times and underutilised at off-peak times.

C&WG also argued that it would have to review all its residential tariffs, including 'Sure Home tariffs', and that in all likelihood all residential customers would face higher prices as a result. C&WG also argued that it would likely result in serious capacity constraint issues if the other OLOs would decide to send UK bound traffic via C&WG in order to get a lower average ppm interconnection rate.

Taking into account all submissions, the OUR set out in the Draft Decision its intention to move to flat rate charges for interconnection services.

Responses to the Draft Decision

In responding to the Draft Decision no party provided the OUR with additional evidence or submissions on the time of day gradient. Whilst C&WG reiterated its objection to removing the gradient, it did not make any additional comments, other than to clarify that a flat rate charge would apply to all interconnection call services.

The other OLOs confirmed their agreement with the OUR's proposal. Wave stated that it anticipated there would be very little change in network usage as a result of moving to flat rate RO charges.

4.2 The charging for interconnection link services

In the draft decision, the DG considered two issues relating to the charging for interconnection link services: the initial charges for new links provisioned between C&WG and an OLO; and the ongoing rental charges for links.

With respect to the former, in the consultation the DG asked whether it would be more appropriate to charge interconnection link services purely on a time and materials basis rather than the current approach based on a fixed upfront price.

The main advantage of an approach based on time and materials is that it better reflects costs, given the bespoke nature of each interconnection link. However, as observed by the respondents to the initial consultation there are also a number of disadvantages. C&WG pointed out that it could be difficult to provide a cost estimate to interested parties and that it might lead to disputes, should there be a significant difference between an initial estimate and the actual costs.

In responding to the consultation one of the OLOs clearly indicated that it preferred the current approach as it provides cost certainty and enables the OLO to budget accordingly. It also argued that charging on a time and materials basis could give C&WG the opportunity of allowing time to slip outside of the agreed timescales with additional charges raised for the work undertaken. The other OLO argued that given the bespoke nature of these type of services a time and materials approach would be more appropriate. However, this OLO did consider that transparency would be very important to enable the OLO to verify that charges are reasonable.

Draft decision

Taking into account all the views expressed by respondents, the DG proposed in the draft decision to maintain the current approach for setting the tariffs for interconnection link services. That is, the DG concluded that a fixed upfront price should continue to be included in C&WG's RO.

In the draft decision the OUR also considered the appropriate level and structure for the ongoing rental charges for interconnection links, and set out a series of principles which C&WG should follow when it calculates these charges. These were as follows:

- The charges should enable C&WG to recover efficiently incurred costs in the provision of interconnection link services;
- Both C&WG and the OLOs should have certainty over the level of charges, which should be set in a transparent manner;
- Where charges are split between ongoing rental and upfront charges, C&WG should ensure that the initial charges do not act as a barrier to OLOs entering the market, whilst also ensuring that C&WG is able to recover its costs;
- Where asset costs are recovered upfront, C&WG should not continue to charge an ongoing rental charge associated with these assets, other than to cover maintenance; and
- Costs associated with interconnection link services should be clearly separated in C&WG's costing system, so to ensure that these costs are not also allocated to other regulated services.

Responses to the Draft Decision

No party objected to the DG's proposed approach. For example, Wave supported the proposal as it would provide OLOs with cost certainty. Whilst Airtel had previously favoured a 'time and materials' approach, it did not object to the OUR's draft decision, on the basis of the relatively low number of interconnection link installations.

In addition, no party objected to the DG's proposed approach for calculating ongoing rental charges for interconnection links. Airtel stated that it assumed the OUR would regularly monitor the basis on which C&WG justified the ongoing rental charges.

4.3 The relative level of proposed charges

The initial consultation published in June 2009 contained a draft set of interconnection rates proposed by C&WG. In the Draft Decision, the DG concluded that rates should be calculated using C&WG's most up to date cost accounting information, namely its 2008/09 regulatory accounts, which were due to be published later in 2009.

Nevertheless, in responding to the Draft Decision, both OLOs raised issues related to the level of the charges. Airtel reiterated its concern (expressed in its response to the consultation) regarding the proposed increase in call termination charges on C&WG's fixed network and sought an opportunity to review the impact assessment of the proposed rates, prepared by C&WG.

In its response to the Draft Decision, Wave noted that C&WG's 2008/09 regulatory accounts (which were published during the consultation period) showed an increase in the average cost per minute for interconnection services (with the exception of off-island transit), compared to C&WG's prior year accounts.

The OUR notes the OLOs concerns and observations in this area. However, the OUR's review of C&WG's proposed interconnection charges and regulatory accounts for 2007/08 concluded that C&WG's regulatory accounting system (on which the proposed charges set out in the consultation were based) did allocate costs appropriately to products.

With respect to the relative level of origination and termination charges, on-island termination rates have historically been below origination rates as a result of the approach taken to calculate these charges. Charges for both services have been based on the unit costs of the network components used by call origination and termination and the relative usage of each component by calls originating and terminating on C&WG's network (i.e., routing factors). These routing factors have taken account of both the call origination and termination services C&WG provides to OLOs and the services it provides to its own downstream businesses (such as C&WG Mobile).

Calls terminating on C&WG's fixed network from OLOs typically use more of C&WG's fixed network than calls which terminate from its own mobile business. This is because C&WG's mobile network interconnects with its fixed network at both exchanges, whereas each OLO's network currently only interconnects at one exchange. Mobile to fixed calls which are originated on C&WG's mobile network are therefore carried relatively more on its mobile network than mobile to fixed calls originated on OLO networks are carried on mobile networks. That is, within C&WG's fixed network, the routing factors for calls terminating on C&WG's fixed network from OLO mobile networks are higher than the routing factors for calls terminating on C&WG's fixed network from its own mobile network. This means that as OLO's market share of mobile traffic has increased, so has the average fixed network routing factor for on-island termination on C&WG's fixed network. This led to the proposed increase in call termination rates.

In determining the final level of charges (i.e., those using 2008/09 costing data), the OUR has conducted a further review of C&WG's cost allocation rules. This has led to a reduction in the unit cost for RO services (and hence RO charges) compared to those set out in C&WG's published regulatory accounts for 2008/09.

4.4 Other issues raised in the Draft Decision

The DG set out two other proposals in the Draft Decision. These were as follows:

- That information on the time of day gradient should no longer be included in C&WG's regulatory accounts; and
- That C&WG should closely involve OLOs in its plans for migrating to NGN.

No objections to any of these proposals were raised by respondents. Further, no other issues were raised by respondents to the Draft Decision.

5. Director General's Final Decision

In this chapter we present the DG's final Decision on C&WG's RO charges. Section 5.1 presents first the DG's Final Decision on the structural and methodological issues upon which he has consulted. Section 5.2 then presents the final RO charges. These have been determined by C&WG, and reviewed by the OUR, using the most recently available cost data and are consistent with final decisions presented by the OUR in this document.

5.1. Methodological issues

Time of Day gradient

The DG considers that there are compelling reasons for abolishing the Time of Day gradient in calculating interconnection charges.

Generally speaking, it is important to ensure that prices accurately reflect the underlying costs of providing the service in question. This provides appropriate price signals to business customers and consumers alike and ensures best use of scarce resources. Network capacity requirements are driven by demand in the peak period and therefore relatively higher peak charges could be reasonable. Furthermore, if a time of day gradient reduces demand in peak periods and increases demand in other periods it avoids a situation where a network operator has to invest in new capacity to meet peak demand whereas there is still excess capacity available at off-peak times. For these reasons, a tariff gradient is typically applied to interconnection (and retail) services offered over communications networks.

However, in deciding whether a tariff gradient remains appropriate in this case it is important that the DG takes into account how the situation in the Bailiwick differs from that in other jurisdictions. In the Bailiwick there are no network capacity issues and forecast traffic volumes are declining. There is therefore no need to smooth demand in order to avoid new investment to meet peak demand for capacity. Given that the majority of peak period traffic is originated by businesses it is also not clear the extent to which the gradient has actually affected traffic patterns.

Furthermore, it is important that the DG ensures that there are no unnecessary obstacles to the development of competition. It is therefore of particular interest that both OLOs argue for flat rates. It is possible that a flat rate for charges in C&WG's RO could further increase competition for the business market as it will reduce the peak period interconnection charges paid by OLOs.

C&WG has argued that abolishing the TOD gradient would favour business customers and penalise residential customers. The DG does not consider this to be the case. The DG does recognise that it could mean that prices for off peak calls might increase in price, relative to calls in the peak period, if operators, including C&WG, were to pass the cost differentials to their customers. However, it could also lead to operators introducing new and innovative pricing structures, thus benefitting consumers.

The DG also notes that C&WG has not been able to submit any evidence that such a change would result in physical network constraints. Furthermore, the DG would have expected that if there was a significant concern about peak demand on the network that local calls would not have been priced at a flat rate.

The DG requires C&WG to adopt a flat rate for interconnection services from 1st April 2010 onwards. Further, C&WG should no longer include information on the time of day gradient in its regulatory accounts.

The charging for interconnection link services

Taking into account all the responses received to both the Consultation and the Draft Decision, the OUR concludes that the current approach to determining the charges for interconnection joining services should remain in place. The OUR believes that this will give certainty to the market and will provide incentives for C&WG to tightly control its costs.

The DG requires C&WG not to change the approach for charging for interconnection link services. This should apply to both the connection charge for new links and the ongoing rental charges for existing links.

NGN

Finally, the DG requires C&WG to involve the OLOs, as its main customers, in the planning of its NGN.

5.2. Revised interconnection charges

The following table presents the updated Reference Offer charges. These shall become effective from 1st April 2010. No retrospective charging shall apply. These charges are based on C&WG's audited cost data for 2008/09, amended to reflect a series of changes to that cost data agreed between C&WG and the OUR to ensure that the charges are cost oriented.

In accordance with his decisions in Section 5 of this Report the DG hereby directs C&WG under section 10(3) of the Telecommunications (Bailiwick of Guernsey) Law 2001 to comply with the decisions set out in this Report. The revised interconnection and access charges are to be applied from 1st April 2010.

Rates Effective 1st April 2010

SERVICE	Pence per call	Pence per minute
On-Island Termination		0.428
On-Island Origination		0.472
On-Island Origination (with Operator Assistance)	169.262	0.842
On-Island Transit		0.299
Off-Island Transit		0.481
On-Island FreePhone Origination		0.472
On-Island LocalCall Origination		0.472
Calls via operator	169.262	0.986
Local Reverse Charge	231.062	0.919
Local Premium Information Services		0.337
Weather Forecast - Guernsey Bailiwick	5.000	0.337
Guernsey Met. Office Info Line		25.466
Time	6.000	0.481
Alarm	230.223	0.804
Emergency Services		170.104
Directory Number Inclusion	per entry	£2.11
Data Management Amendments	per hour	£55.41

Customer Sited Interconnect

New Carrier System	**Installation cost**	**Quarterly rental cost**
Per System including initial 2 Mbit circuits	£38,599.92	£1,312.02
Ducting and cabling per metre		£97.86

(minimum 20m up to 70m total))		
Ducting and cabling per metre (more than 70m in total))		£94.04
Additional 2Mbit links	£1733.28	£656.01

In-Span Interconnect

New Carrier System

	Installation cost	**Quarterly rental cost**
Per System including initial 2 Mbit circuits	£29,425.41	£1,312.02
Ducting and cabling per metre (minimum 20m up to 70m total))		£97.86
Ducting and cabling per metre (more than 70m in total))		£94.04
Additional 2Mbit links	£1733.28	£656.01

6. Conclusion

The DG has now completed his review of C&WG's RO rates and these have now been applied by C&WG. The DG would like to thank all parties for their co-operation in assisting the OUR with this review. The revised RO, including rates, may be found on C&WG's website - www.surecw.com/guernsey/page-1648.

ENDS

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