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network separation the italian case

AGCOM

*Italian
Regulation Authority*

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Setting the scene

- In Europe, the current legal framework for regulating market power empowers the NRAs (National Regulatory Authorities) to impose ex ante remedies (regulatory obligations) on operators having Significant Market Power in the markets listed by the Commission
- The remedies imposed on SMP operators shall be based on the nature of the competitive problem identified, proportionate and justified in the light of the regulatory objectives laid down in article 8 of the Framework Directive
- Remedies are *numerus clausus*. Extra ordinem measures under exceptional circumstances may be submitted to the veto power of the European Commission

Setting the scene

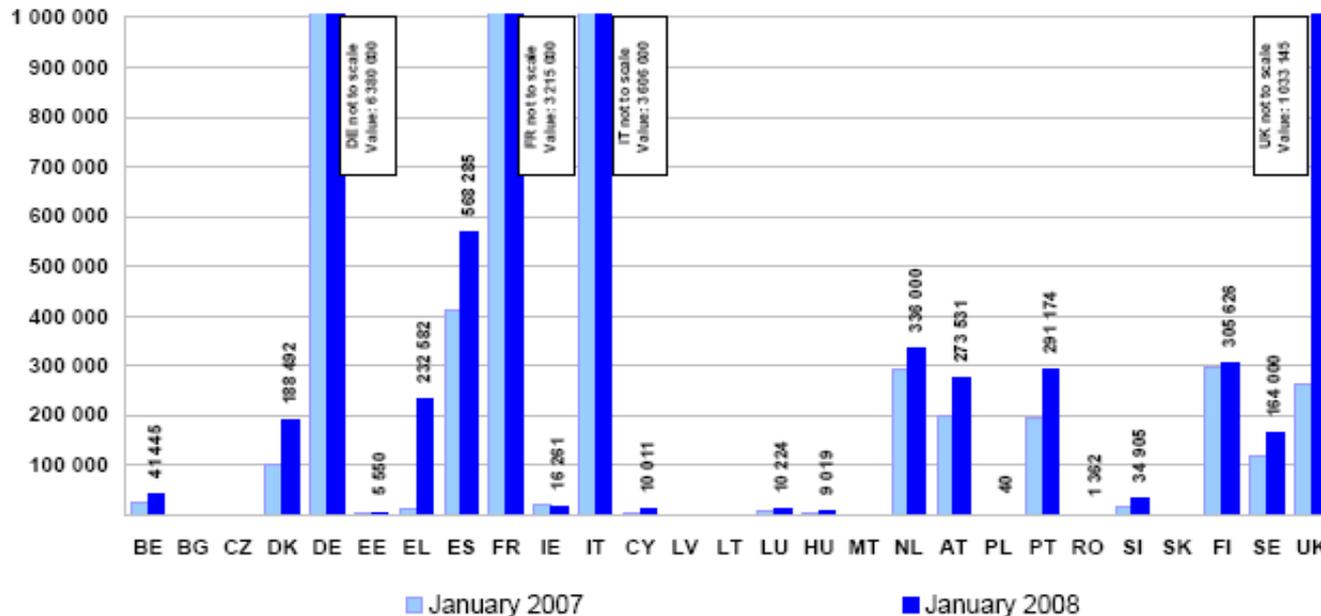
- Key concerns about competition stem from wholesale access to bottleneck facilities. Indeed, following the first round of market analysis, Agcom found Telecom Italia (TI) as having SMP in the wholesale access network market (market n. 4). The main competition problems revolve around:
 - Vertical leveraging (margin squeeze; discrimination in provisioning and assurance; handling of OLO's business sensitive information)
- Overall, pro-competitive remedies had to face the "triple" challenge of balancing:
 - i) competition;
 - ii) efficient scale of investment
 - iii) consumer welfare

More in detail: the first regulatory period

- The so-called standard remedies, transparency, cost-oriented, non discriminatory obligations and accounting separation have proved successful
 - accounting separation offered effective tools to tackle the risk of price discrimination between Telecom internal divisions and OLOs' business units which purchase Telecom's wholesale access products:
 - price tests guarantee replicability by OLOs of Telecom's retail offers which hinge on regulated wholesale services
- Telecom Italia's market share decreases steadily without the pressure of dual mode competition since in Italy there is no cable network
 - Significant price reduction at retail level

More in detail: the first regulatory period

- The most important wholesale access product is ULL
 - *“Italy remains one of the EU leaders in local loop unbundling (LLU). As of January 2009, there were 4.7 million active full LLU lines (+ 31% with respect to January 2008)) and around 556 000 shared access lines.”* (14th Progress report on the single european electronic Communications market)

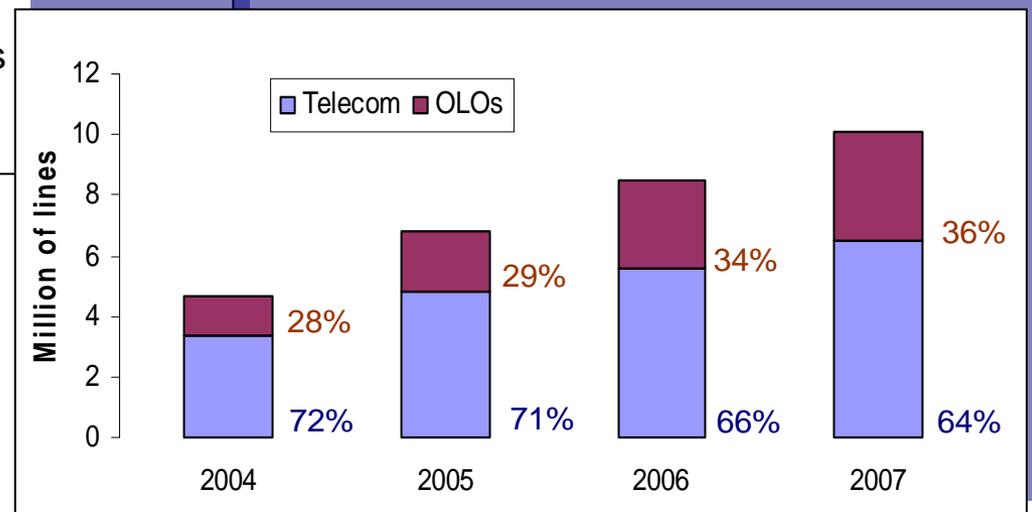


- Bitstream and WLR (logical /broadband access) are second best options

More in detail: the first regulatory period

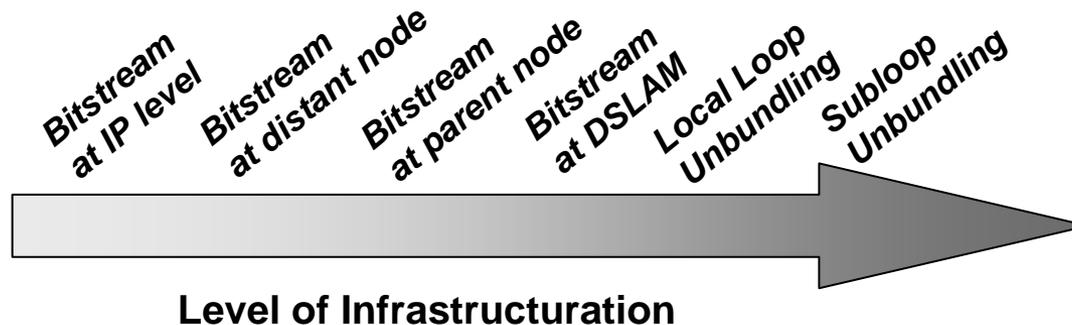
■ TI's market share

-  Access revenues: 85.7%
-  Telephony revenues: 61.7%
-  Access + Telephony revenues: 75.9%
-  Broadband lines: 64%
-  incumbent's market share on DSL lines (97% of BB lines): 65.8%



More in detail: the first regulatory period

- Overall, the pro-competitive regulatory environment has warranted the:
 - promotion of infrastructure-based competition on a gradual basis
 - ladder of investments



Dealing with shortcomings: the second regulatory period

- The regulation of wholesale access products offered by Telecom Italia proved successful for the launch of competition but...
- it failed to address complaints of non – price discrimination caused by abuse of the advantages of vertical integration

Dealing with shortcomings: the second regulatory period

- Evidence of market foreclosure attained through non-price discrimination:
 - Deny, detail, degrade... such conducts are difficult to detect and deal with through standard remedies
 - Telecom's personnel was not discouraged to pursue non-price discrimination practices
- High costs of non-price discrimination
 - Enormous amount of litigation between Telecom and OLO
 - OLO's business plans affected by the lack of information and transparency
 - Poor quality of services for OLO's final users
 - First mover advantage in the launch of new products (high speed adsl)

Towards new solutions

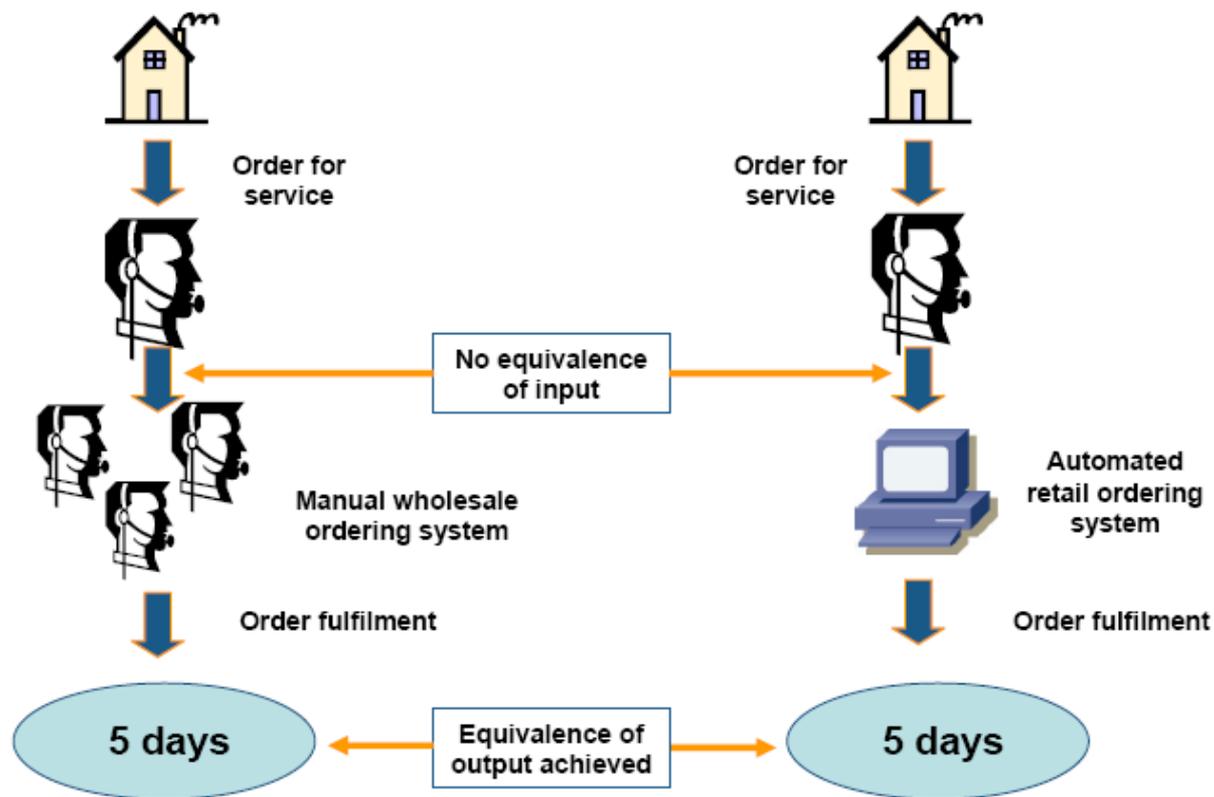
- Administrative separation, enacted by Agcom in the first regulatory period (since 2002), based on accounting separation and complemented by standard remedies (regulatory obligations), urged to be reinforced. Arm's length rules were circumvented
- Regulatory dilemma: tackling non-price discrimination without hindering the:
 - Drive for investment;
 - Internal coordination
- Striking a balance between the advantages of vertical integration and a model of separation focused on non-price discrimination

Operational separation

- Operational separation was elected as the best solution
- It relies on a mix of equivalence of input and of output
- Where a strict equivalence of input was impossible or too expensive to achieve equivalence of output is warranted
 - The goal is to ensure that OLOs are treated equivalently to the incumbent's internal divisions in product, service delivery and in pricing
 - Equivalence of input requires processes to be exactly the same between internal divisions and competitors. The stress is on the source.
 - Equivalence of output demands that the wholesale products that incumbent offers to its wholesale customers are the same to those that it offers to its own units, irrespective of the procedure followed to deliver them. Stress here is on the outcome.

Operational separation

- Equivalence of output does not demand necessarily equivalence of input



The Italian way to operational separation

- The Italian regulator is not vested with the power to impose separation on Telecom Italia, neither by municipal or by EC law
- Italian Act n. 248/2006 allows regulated firms to submit a proposal of undertakings in proceedings pending before the regulator which affect competition. If accepted by the regulator, such commitments become mandatory for the submitter
- Telecom Italia, on a voluntary basis, has submitted a proposal of operational separation (Undertakings)

The Italian way to operational separation

- The submission of the Undertakings was triggered by the fear of heavy fines in a number of infringement proceedings opened by Agcom against Telecom Italia for anti competitive practices.
- TI Undertakings were submitted for public consultation
- Agcom conditioned its agreement to several changes in order to make the Undertakings more effective to enhance competition
- The Undertakings, in the amended version, were approved by Agcom

Open Access

- Telecom Italia operational separation sets out:
 - Creation of **Open Access**, a new Division in charge of the passive elements of the access network: the copper access network (local loop from the local exchange to the street cabinet; sub-loop from the street cabinet to the end-user premises; street cabinets; MDFs); the fibre access network; the local backhaul network (copper and fibre)
 - Overhaul of of the **Wholesale Division** dealing with OLO's demand for network access services and network maintenance (one-stop shop)
 - A number of **commitments** addressing:
 - **Non- discrimination**
 - New delivery process: mandatory implementation of a first-come first served process
 - Incentives for the management of Open Access and of Wholesale Division rewarding equality of treatment of the OLOs and TI

Open Access

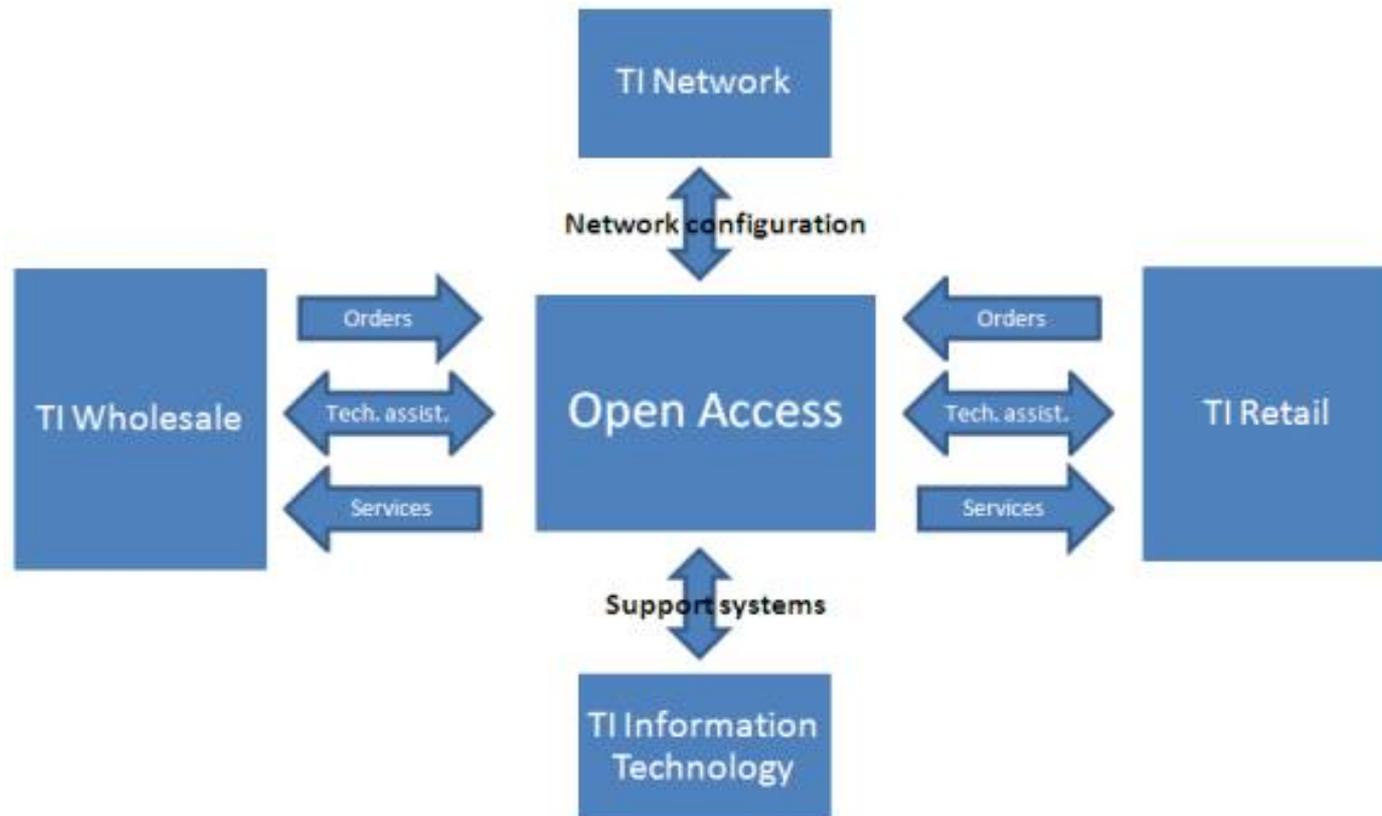
- Comparison of internal and external supply performance through Key Performance Indicators (KPIs) monitoring
 - Prices charged by Open Access to TI retail (internal transfer charges) submitted to AGCOM for approval
 - Separate accounting framework for Open Access, providing sufficient detail to allow the assessment of equivalence between transfer charges and the prices charged to other Operators
- Performances
- New delivery process: multiple queues for requests of different priority (all using first-come, first-served process); requests can be held in system until they are fulfilled (no more need to resubmit activation requests that fail); further information can be attached to activation requests by OLOs (level of quality, pre-arranged date for technician visits, special delivery needs)

Open Access

- Incentives for the management of Open Access and of Wholesale Division rewarding quality of services
- New Customer Relationship management (CRM Wholesale) offering a better service
- New monitoring system: integration of currently mandatory KPIs, Key Performance Objectives jointly defined with AGCOM every year
- **Transparency**
 - Monthly, quarterly and annual reporting on performances (reports submitted to Agcom and supervisory board and published on TI website dedicated to OLOs)
 - Detailed technical planning information made available to OLOs
 - Detailed quality improvement planning information made available to OLOs
- A supervisory board is in charge with the task of guaranteeing the enforcement of the Undertakings. Three out of five members of the board are appointed by Agcom. They are vested with the power of inquiry and report.

Open Access

- Open Access receives orders for access network services from both 'TI Wholesale' and 'TI Retail', and serves alternative operators and TI's own retail customers



Open Access

- Offer of services: it includes *bitstream* services differently from the British separation

<i>Service</i>	<i>Open Access (IT)</i>	<i>Openreach (UK)</i>
<i>Unbundling</i>	<i>Yes</i>	<i>Yes</i>
<i>Bitstream</i>	<i>Yes</i>	<i>No</i>
<i>WLR</i>	<i>Yes</i>	<i>Yes</i>
<i>Leased Line Products</i>	<i>Yes</i>	<i>Yes</i>
<i>Backhaul Products</i>	<i>Yes</i>	<i>Yes</i>

TI's Undertakings and NGN: looking forward

- The submission of the Undertakings has officially opened the debate on the roll-out of the new generation network - NGN
- Agcom required Telecom to accept:
 - The membership of Telecom Italia in the NGN Committee established by AGCOM. The Committee is called to steer the debate among the stakeholders about discuss technical, economic and management issues
 - TI will publish a reference offer (fair and reasonable prices) for access to its passive infrastructures (ducts). In case access is not possible or economically viable, TI has to provide dark fiber (same conditions as above).
 - TI will publish a proposal for sharing and joint building of new infrastructures.

TI's Undertakings and remedies

- Undertakings and operational separation claim legal grounds in national regulation and do not clash with EU legislation
- The forthcoming results of market analysis are going to evaluate the pro-competitive effects of the Undertakings.