Telecom Italia’s undertakings: building up an operational separation model

Workshop on “NETWORK SEPARATION: Models, Economics and Regulatory Implications”

Columbia University, New York, 26th March 2009
Equivalence and Regulatory Affairs

MISSION

► Managing the regulatory process to increase the company’s value by affecting market changes in the mid-long term.

VISION

► Leading the change, as an influential team and a strategic reference for the company in the development of its business and in consumer protection; establishing a loyal dialogue with the other market players, Authorities and Institutions for the achievement of a simple, efficient and symmetric regulation.
The role of vertical separation remedies

► It is well known that standard remedies (access obligations, price control...) might fail in some circumstances to address the competition problems raised by vertical integration (non-price issues may be particularly difficult to be tackled).

► In case an NRA maintains – on the basis of concrete market evidence - that standard remedies in place have failed, and are bound to fail in a forward-looking perspective, to address the competition problems raised by vertical leveraging of significant market power in the access network, “exceptional” vertical separation remedies may be considered.

► The separation of the fixed access network from the retail activities can be marked by several intensity degrees related to their effects on vertical integration:
  ► Accounting Separation;
  ► Operational Separation schemes (including Functional Separation);
  ► Legal Separation;
  ► Ownership Separation.
Overview of Telecom Italia’s Operational Separation

- Regulatory provisions concerning the equality of treatment introduced in 2002
- Creation of Open Access in 2008
- Telecom Italia’s Operational Separation Model
- Legally binding Undertakings entered into force as of 1° January 2009
Regulatory provisions concerning the equality of treatment introduced in 2002

- It is not widely known that the very first case of enforcement of organisational remedies by a European NRA has been the regulation introduced in 2002 by AGCom Decision 152/02/CONS (on the basis of the Italian law n. 481 dated 14/11/1995).

- As a consequence of the new regulation, the following main vertical separation remedies and organisational measures were introduced:
  - physical separation of TI wholesale staff and management from TI retail ones;
  - logical/physical separation of network/wholesale systems from the retail systems aiming at avoiding access to OLO’s data by the retail units (more than 60 information systems were taken apart);
  - introduction of KPI in order to monitor the equality of treatment in the provision of regulated wholesale services.
Trends of Telecom Italia’s wholesale access services

Almost 4 millions unbundled lines at the end of 2008

Direct-access competition (LLU+SA) is overcoming indirect-access competition (CS+CPS+WLR+Bitstream)

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Direct-access competition (LLU+SA) is overcoming indirect-access competition (CS+CPS+WLR+Bitstream)
The creation of Open Access (1/2)

The Open Access business unit has been created at the beginning of 2008

- to achieve efficiencies both in operational and maintenance costs and network investments; and
- to increase transparency in the provision of wholesale access services to TI’s commercial departments and to the alternative Operators (OLOs) by means of TI’s Wholesale department.

Open Access manages TI’s access infrastructures and provides the following main services:

- Copper physical link supply between client and local exchange for TI and OLO
- Wholesale Line Rental (WLR) service
- Co-location service supply in the central exchange spaces
- Optical fibre physical link supply
- Maintenance services on copper and fibre links
- Access to ducts
- Wholesale broadband access (bitstream services)
The creation of Open Access (2/2)

Open Access plays a key role in ensuring the implementation of TI’s undertakings due to the fact that most of the undertakings concern the equivalence in the provision of SMP network access services produced by Open Access. Therefore, Open Access is the organisational tool to achieve access equivalence for both TI retail divisions and OLOs.

For these reasons, even if the creation of Open Access is not part of TI’s Undertakings, any significant organisational change of both Open Access and TI Wholesale, is to be previously submitted to AGCom approval.
Main objectives of TI’s Undertakings

On 15th December 2008, AGCom approved TI’s Undertakings (Decision 718/08/CONS):

► 223 undertakings are legally binding as of 1st January 2009.

TI’s Undertakings are intended to:

► strengthen the operational separation model by addressing the competition concerns expressed by AGCOM;
► reduce the degree of litigation with OLOs;
► ensure competitive conditions in the migration towards new generation networks.

TI’s Undertakings are not intended to modify current regulatory remedies imposed by AGCom on TI.

The undertakings have been voluntarily added by TI to the current remedies.
14 Groups of undertakings: an overview

9) Access to ducts and dark fiber offers (in case of technical difficulties); equivalence for SPM services on NGAN; joining NGN Italia Committee; “migration” plan proposal

6) Ensuring transparency of the “Next Generation Access Network Plan (NGN 2)”

EQUIVALENCE

1) SPM Services’ Delivery; Co-location; wholesale CRM
2) Code of Conduct
3) KPI monitoring system
4) KPI transparency
5) Network Quality Plan Transparency
6) Network Development Plan Transparency
8) OA’s Separate Accounts and fixing of Transfer Charges

GOVERNANCE

7) Supervisory Board
10) Joining the Office of Telecom Adjudicator

CONSUMER PROTECTION

11) Ban on commercial activities for OA network technicians
12) Unsolicited services’ activation reporting
13) CPS termination procedure
14) More efficient dealing with complaint and reducing disputes with consumers
Ensuring Technical Equivalence: the new single delivery process for the provision of access SMP services

The new single delivery process aims at:

▶ improving internal/external equal treatment in the production and provision of SMP Services;

▶ handling orders, without discriminating between internal and external ones, with the introduction of different “queues” based on:
  
  ➢ type of service;
  
  ➢ level of quality chosen at the order;
  
  ➢ reception time (first come first served).

In case of network resource unavailability, upon request, OLOs’ orders will be held in a waiting system based on a “single-queue” and will be automatically processed when the network resource becomes available.
Ensuring Technical Equivalence: the new monitoring system on equal treatment

Current mandatory indicators, imposed by Decision 152/02/CONS, only measure service performance on an end-to-end basis.

The new monitoring system will focus on Open Access’s activities by comparing KPIs related to the wholesale phases of SMP services delivered to TI Retail (KPI $\alpha$) with KPIs related to the production of the SMP Services delivered to OLOs (KPI $\beta$). KPIs are to monitor delivery, assurance, service availability and supporting systems quality. Relevant KPOs are to be agreed with AGCom.
Ensuring Economic Equivalence

**Introduction of Internal transfer charges for SMP access services**

TI is to elaborate and submit to AGCom approval a proposal of internal service contracts based on the economic transfer charges related to the provision of SMP services delivered by Open Access.

**Integration of TI’s Regulatory Accounting to include Open Access**

TI is to elaborate and submit to AGCom approval a proposal for a separate regulatory account system related to Open Access.

The new accounting separation of Open Access will provide evidence concerning the equivalence between the transfer charges applied to the internal commercial divisions and the relevant economic conditions applied to alternative operators.
Ensuring Access Equivalence to Next Generation Access Networks

**Access to ducts and dark fibre**

TI will provide an offer for the access to and sharing of its ducts. If this access is neither technically possible nor economically viable, TI is to provide an alternative solution based on access to dark fibre. Open Access will directly manage the creation of a new system to allow the delivery of the ducts offer directly to OLOs.

**Access equivalence to NGAN**

With reference to the second round of AGCom market analysis, the current undertakings shall be extended to all the new wholesale network services, provided over the NGAN, in which Telecom Italia will be found as having SMP.

**Migration process**

Also on the basis of the discussions within the “NGN Italy Committee”, TI is to submit to AGCOM’s approval a proposal of guidelines for the migration process towards NGAN and the phasing out of some TI local switches.

**Transparency on NGAN development plans**

TI undertakes to release the “New Generation Access Network Plan (NGAN)”, which is to outline the percentage of new generation lines for each local exchange area and municipality, with reference to the so-called “passed home”. In addition, it will include technical information on wholesale services, if any, which might become locally available on the new network platform.
Ensuring achievement of equivalence: the Supervisory Board

Telecom is to set up an internal independent body (“Supervisory Board”) in charge of supervising and verifying:

- the proper implementation of the Undertakings;
- the compliance of Key Performance Indicators (KPIs) with the principles of equal treatment and quality objectives in the supply of fixed network access services.

The Supervisory Board is composed of five members appointed by Telecom. Three members, including the President, are designated by the Authority. All members must be independent from Telecom, other electronic communications operators and television operators.

The Undertakings and the Regulation of the Supervisory Board ensure that the latter has access to all information necessary to the performance of its monitoring activities.

The Supervisory Board can require expert opinions, statistical and economic analysis or consulting services, with regard to any aspect relevant to the performance of its tasks.

The Supervisory Board can also receive reports and complaints from alternative operators and other third parties, with regard to potential anomalies or inadequacies in:

(i) the implementation of the Undertakings; and
(ii) the values of the KPIs.
Time schedule and cumulative number of Undertakings to be implemented

67% of TI’s Undertakings implemented by 1st April 2009

+ 3 undertakings whose implementation time depends from AGCom
Telecom Italia’s Operational Separation model: main features

- Creation of a separated business unit – Open Access – providing SMP access services both internally and externally.
- Physical separation of Open Access and TI Wholesale staff and management.
- Separated incentive schemes and separated code of conduct for Open Access and TI Wholesale staff and management.
- Logical/physical separation of information systems.
- Technical equivalence for both existing and forthcoming SMP access services based on the equivalence of output concept.
- Economic equivalence based on internal contracts and internal transfer charges consistent with regulated wholesale prices.
- Governance of the equivalence model ensured by the Supervisory Board.
A comparison between the Operational and the Functional separation models (1/4)

The main differences between the operational separation model that will result from the adoption of the Undertakings by TI and the functional separation model adopted by BT can be found in the following areas:

- approach to the non-discrimination in the provision of access services;
- governance of investments in the Access Network.
A comparison between the Operational and the Functional separation models (2/4)

Non-discrimination in the provision of access services

BT Model

► A single system for the delivery of the access network services, both to the OLOs and to BT Retail: the so called “equivalence platform”. Being the same system, the internal-external equal treatment is ensured by definition.

► The model adopted by BT requires extensive investments to redefine all the operating systems. From the point of view of the access network delivery, Open Reach operates as it were in actual fact a separate entity.

TI Model

► Maintenance of two different systems for the delivery of the access network services:
  ➢ one for TI Retail;
  ➢ another for the OLOs, managed by TI wholesale.

► Under the Undertakings the two systems are and will remain subject to strict equal treatment rules. The single new delivery process of SMP Services ensures complete equal treatment in the access to network facilities.
A comparison between the Operational and the Functional separation models (3/4)

Governance of investments in the Access Network (1/2)

BT Model

- Separation in the UK means that technical information can flow within BT, but not commercial information: no sharing of commercial information between BT Wholesale, Openreach and BT’s retail units.

- The Undertakings do not make coordination of the relevant information impossible, but they do make it more difficult because this coordination is carried out with a high level of consultation among a variety of stakeholders which removes some of the benefits and efficiencies emerging from coordinated decision-making.

TI Model

- Vertical integration enables the efficient flow of information among retail, network, access and other company’s units to ensure efficient planning of the investments. For the NGAN deployment, information is shared among the network, access and retail units.
A comparison between the Operational and the Functional separation models (4/4)

Governance of investments in the Access Network (2/2)

BT Model

- In the Openreach-style environment, the “Access” unit will not take into account those cost savings not accountable to itself and must take every investment decision purely on its merits regardless to the commercial interest of other parts of BT Group.

TI Model

- Cost savings from TI’s investments in NGAN may be shared between the access network and other parts of the network allowing for an optimal design of the new network.
Impact of TI’s Undertakings on competition and on the evolution of regulation

Similarly to the functional separation implemented by BT, the operational separation model of the access network introduced by TI will promote competition in downstream markets by:

► promptly implementing effective technical and economic “equality of output” conditions between TI’s retail functions and OLOs;

► removing any possible competitive risk associated with the incumbent’s vertical integration.

AGCom Decision 718/08/CONS stated that TI’s Undertakings “are suitable to structurally improve the competitive setting of the markets affected by the undertakings”.

AGCom is to assess - in the market analysis proceedings - the competitive impact of TI’s Undertakings on each specific relevant market, in order to determine whether to impose, maintain, amend or withdraw obligations according to the provisions of the European regulatory framework.
Telecom Italia’s Operational Separation model: concluding remarks

- Telecom Italia’s Operational Separation model aims to ensure an effective “equivalence” in the delivery of SMP access services to alternative operators by means of an efficient implementation of the equivalence of output concept.

- Telecom Italia believes that its Operational Separation model is:
  - as effective as the Functional Separation model in achieving an excellent non-discriminatory framework;
  - less expensive in terms of required investments and implementation costs.

- Telecom Italia’s Operational Separation model carries on the company’s vertical integration, allowing for an efficient flow of information among retail, network, access and other company’s units. Accordingly, efficient planning of investments, including NGAN, is ensured.