



Wholesale Pricing Guidelines for ICT Sector for SADC

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1 INTRODUCTION

1.1 Background

The Southern African Development Community (SADC) Protocol on Transport, Communications and Meteorology is the basis for providing direction to development of the communications sector in the region. Amongst others, the Protocol provides the regulatory authorities with the responsibility to develop and determine harmonized guidelines and regulations for the region.

In the “Declaration on Information and Communications Technology”, signed by the Heads of all the SADC countries in August 2001, it is recognised that SADC needs a coherent regional policy and strategy on Information and Communications Technologies (ICT)¹ that promotes sustainable economic development, technology and bridges the digital divide within the region and rest of the world.

The Declaration on ICT acknowledges that effective information and communication is best achieved under an environment characterized by e.g. policy guidelines, legislation, well defined strategy and telecommunications deregulation.

Further, it is declared that the SADC Member States undertake to continue to sustain efforts “in creating a favourable regulatory environment and accelerated liberalization of the telecommunications sector, which aims at creating a three-pier separation of power, with governments responsible for a conducive national policy framework, independent regulators responsible for licensing, and a multiplicity of providers in a competitive environment responsible for providing services”.

These guidelines have been prepared to support the development into a competitive and efficient ICT sector in the SADC region for the benefit of the users, through the provision of transparent and non-discriminatory guidelines on wholesale pricing².

1.2 Scope of the Guidelines

The evolving competition in the market imply that new and existing providers need to have arrangements and agreements with each other to guarantee e.g. interconnection and interoperability of networks and services. In practice, a successful development of the sector relies to a

¹ ICT = Information and Communication Technology

² These guidelines on wholesale pricing for the SADC region are based on the analysis, findings and recommendations in the study report on wholesale pricing. The study report is a supporting document to these guidelines. The guidelines are kept rather brief and further details on the considerations and recommendations to the guidelines are found in the study report

large extent on agreements and relationships between the operators and service providers in the market.

Wholesale pricing refers to the compensation for wholesale products, services and associated facilities supplied by one operator to another. In the initial stages of liberalization, the wholesale pricing arrangements are fundamental to the development of fair competition in the sector, since the major operator(s) usually has a significant advantage because it owns or controls essential facilities that new providers need access to on reasonable terms to compete successfully. Even as competition develops the prices for wholesale products and facilities will be highly important since the wholesale prices paid will make up a significant portion of the operators' total costs and revenues.

From a policy and regulatory point of view, there is a need to promote and stimulate wholesale pricing arrangements that lead to fair competition for the benefit of consumers.

The rapid changes in technology and markets lead to an increased convergence between the traditional telecommunications, IT and broadcasting/media sectors. This ongoing convergence needs to be considered when reviewing and analysing market conduct in the sector, including wholesale pricing arrangements.

These guidelines apply to wholesale pricing in the ICT sector, consisting of all electronic networks and electronic services and associated facilities³.

³ The provision of content over electronic networks and by using electronic services, as defined, should lie outside the scope of these policy guidelines and regulations. This will exclude e.g. broadcasting content and electronic commerce from the scope of these guidelines. The main reason for this is that content provision is governed by other laws and regulations where other considerations on e.g. anti-competitive pricing and determinations of essential facilities will apply. The main aim of these guidelines is to provide guidance to a sector in transition from monopoly to effective competition with respect to infrastructure and service provision, and not to provide regulations on content or applications that use the networks and services. See also glossary of terms.

Abbreviations and Acronyms

The following abbreviations and acronyms have been used throughout this document:

FDC	-	Fully Distributed Costing
ICT	-	Information and Communications Technologies
LRIC	-	Long Run Incremental Cost
NRA	-	National Regulatory Authority
SADC	-	Southern African Development Community
SATCC	-	Southern African Transport and Communication Committee
TRASA	-	Telecommunications Regulatory Association of Southern Africa

2 SCOPE OF INTERCONNECTION

2.1 Objectives

The major objective of the guidelines is that SADC Member States shall promote fair wholesale pricing regimes in the ICT market by:

- (a) Ensuring that consumers get the maximum benefits in terms of choice, quality and value for money;
- (b) Ensuring that the wholesale pricing arrangements are efficient; and
- (c) Encouraging efficient investments in infrastructure.

2.2 Principles

The basic principles underlying these guidelines should be as follows:

- (d) Non-discrimination;
- (e) Transparency;
- (f) Cost orientation;
- (g) Sustainability; and
- (h) Technology neutrality.

2.3 Non-Discrimination

The principle of non-discrimination shall ensure that an operator with market power shall give equal treatment to other operators and service providers, and not be allowed to provide less favourable conditions to some parties for the same product or service.

However, any operator may differentiate offerings and wholesale prices provided there are justified conditions to do so⁴.

2.4 Transparency

Regulators and other authorities shall keep their procedures and decision-making processes open to the public. The regulators shall also, whenever reasonable, consult all affected parties on matters that affect such parties.

Operators with significant market power shall, in accordance with the regulators' requirements, provide transparent information that shall be available to other companies and to the public.

⁴ An example of such conditions may be lower unit cost due to higher volumes.

2.5 Cost Orientation

Cost orientation refers to the principle that the prices and charges for wholesale products and services shall be oriented towards the underlying cost of providing them.

2.6 Sustainability

Sustainability requires that wholesale prices be established in a manner that compensates efficient wholesale operators for their wholesale service provision; that is, operators shall have an opportunity to be compensated sufficiently to remain as a going concern over the indefinite future with respect to their provision of wholesale services. The prices set shall be at levels that could be sustained by efficient operators in a fully competitive market. Sustainability, however, does not require full compensation for inefficient or imprudent service provision.

2.7 Technology Neutrality

The principle of technology neutrality shall apply. That is, the application of the guidelines shall not discriminate nor favour any specific technology to the extent that it will benefit the SADC Member States.

3 CATEGORIES OF WHOLESALE PRODUCTS

The wholesale facilities, products and services available and required are dependent on the market development and regulatory intervention.

The following wholesale facilities, products, services and related functions are relevant to these guidelines:

- (a) Access to local loops and other specified unbundled network elements and facilities;
- (b) Access to rights of way, including poles, ducts and conduits;
- (c) Access to technical interfaces, protocols or other key technologies and facilities required for the interoperability of services;
- (d) Access to specified services needed to ensure interoperability of end-to-end services to users, including facilities for intelligent network services and roaming on mobile networks;
- (e) Access to operational support systems and other software systems necessary to ensure fair competition in the provision of services;
- (f) Interconnection of networks and network facilities;
- (g) Leased lines and other types of transmission capacity;
- (h) Telephone numbers, operator services, directory assistance and directory listing;
- (i) Equal access;
- (j) Number portability;
- (k) Collocation and other forms of facility sharing required including duct, building or mast sharing; and
- (l) Bundled retail services provided at wholesale prices for resale.

4 WHOLESALE PRICING APPROACHES

Wholesale pricing covers the compensation between operators and service providers for different wholesale products, services and associated facilities. The pricing approaches used will vary depending on the types of wholesale arrangements and the wholesale products, services and associated facilities provided. The pricing approaches may include, but not be limited to, cost oriented pricing, retail price minus discount factor (i.e. retail price minus avoided cost), revenue sharing, benchmarking and sender keeps all (i.e. bill and keep).

Wholesale pricing that foster fair competition and provide the maximum benefits to the consumers should be promoted. Based on the general principle of cost orientation the following should apply for essential wholesale facilities, products and services:

- (a) Prices should be cost oriented (ideally based on long-run average incremental costs, including cost of capital, plus a reasonable mark-up to cover forward-looking joint and common costs).
- (b) Prices should be based on the current replacement costs of assets (discounted to their remaining service life). In the absence of such costs, depreciated book value of assets should be used.
- (c) Prices should be sufficiently unbundled so that an operator seeking interconnection need only pay for the components or services it actually requests.
- (d) Prices should not include hidden cross-subsidies of an anti-competitive nature, e.g. charges for monopoly-supplied network components should not be inflated to a level well above costs in order to fund below-cost provision of competitive components⁵.
- (e) The structure of prices should reflect the underlying costs⁶.

⁵ This principle is adopted in the WTO Regulation Reference Paper.

⁶ Thus, fixed (non-traffic sensitive) costs should be covered by fixed (non-traffic sensitive) charges, variable (traffic sensitive) costs by variable (traffic sensitive) charges. Peak and off-peak charges may be set where there is a significant difference in costs.

5 CRITERIA FOR INTERVENTIONS

5.1 Introduction

Regulatory interventions covering wholesale prices should only be imposed in markets for products and services that are not workably competitive. The extent and nature of the intervention will vary between providers and services, depending on the extent of market power and potential for associated abuse.

In general, operators with significant market power and control over monopoly facilities and products required in markets for essential retail services will be required to demonstrate an objective basis for cost oriented wholesale prices. Regulatory Authorities imposing obligations on the accessibility and pricing of wholesale facilities, products and services should take account of:

- (a) The technical and economic viability of using and installing competing facilities with consideration to the market development;
- (b) The feasibility of providing the access required in relation to the capacity available;
- (c) The initial investment by the facility owner, bearing in mind the risks involved in making the investment;
- (d) The need to safeguard fair competition in the long run; and,
- (e) Where appropriate and relevant, intellectual property rights.

A determination of which operators should be required to demonstrate cost-oriented wholesale prices should be based on the following process:

- (a) Definition of the relevant market;
- (b) Assessment of market power; and
- (c) Determination on the requirements on one or more operators to demonstrate cost-oriented prices.

5.2 Definition of the Relevant Market

The starting point for imposing obligations on cost-oriented wholesale pricing should be a definition of a relevant market⁷.

⁷ This is in analogy with the process used for assessing anti-competitive practices. Please see "Fair Competition Guidelines for the ICT Sector for SADC" for further details on this process.

5.3 Assessment of Market Power

An assessment should thereafter be made with respect to the market power of one or more firms in the defined relevant market.

5.4 Determination on Requirements

Based on the assessment of market power, a determination should be made with respect to the requirements on one or more operators to demonstrate cost-oriented wholesale prices. In connection to this, an assessment and determination of the essential wholesale facilities, products and services should be made. Due to rapid technological and market changes, such analysis and assessment process should be undertaken on an annual basis.

Operators determined to have significant market power through the ownership or control over essential facilities, products and services should normally be required to demonstrate cost-oriented wholesale prices for such facilities, products and services. The essential wholesale facilities, products and services should be provided at least equal in quality and at no less favourable conditions than those given by the operator to itself or to any other subsidiary, affiliate, or any other party.

6 COST AND METHOD

6.1 Cost Standard

Long Run Average Incremental Costings⁸(LRAIC) based on forward looking costs should be the preferred standard for calculating cost-oriented wholesale prices for key essential wholesale facilities, products and services⁹. LRAIC is intended to mirror the prices that would prevail if the market were characterized by effective competition.

Implementation of the LRAIC may require a transition period in the SADC Member States. The complexity, time and other resources required to implement the LRAIC standard in practice should be taken into full account, necessitating a phased approach to the implementation of LRAIC.

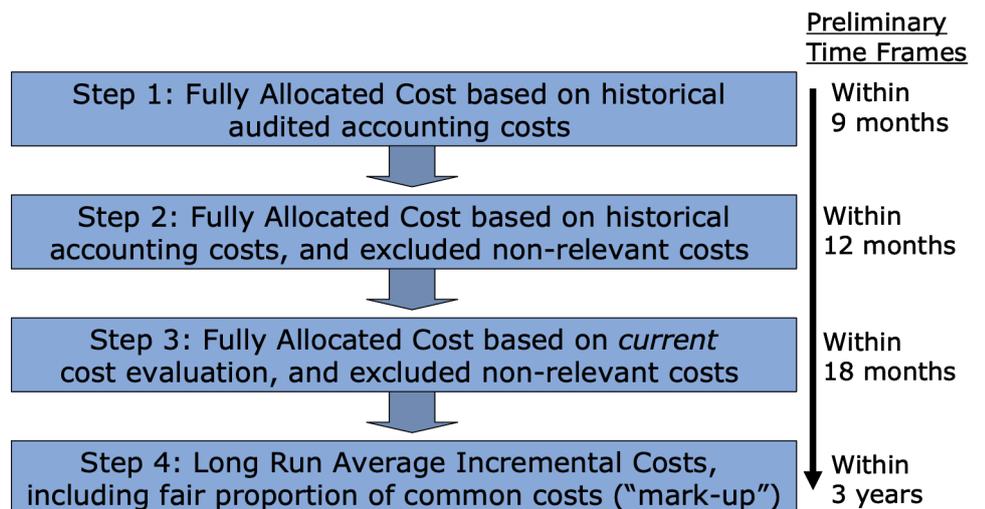
In the short term, the Fully Distributed Costing (FDC) standard based on historical costs should form the basis for calculating cost-oriented wholesale prices. This should only be seen as a temporary solution while preparing for prices based on a current cost valuation which should be used as a proxy for forward looking costs.

The national regulators, in cooperation with the industry, should, based on the following suggested plan, establish a time and action plan for the process forward in each SADC Member State while taking into account the specific situation and development in the SADC Member State¹⁰.

⁸ Long run incremental cost (LRIC) is the incremental costs that arise in the long run with a specific increment in volume of production. LRAIC is a version of LRIC. The term “average” captures the intent to define the increment as the entire service. LRAIC includes service-specific fixed costs. See also glossary of terms.

⁹ A typical key essential wholesale product in the current market transition to workable competition is switched interconnection. However, in practice it is not reasonable or realistic to require that all essential wholesale facilities, products and services have to be separately calculated based on the prescribed cost standard. Hence, the regulatory Authorities need to set realistic requirements on the level of detail of costing, and put focus on the most important and critical essential facilities, products and services, such as, currently, interconnection services.

¹⁰ Some countries in the SADC region may already have completed one or two steps in the process and are therefore likely to be in a position to move forward quicker than what the preliminary time plan suggests. It is important that the time and action plan finally agreed upon between the national regulator and the affected operators recognize that the output of one step in the process is not a pre-requisite to initiate activities in the next step. For example, the work to reevaluate the assets into current costs could and should be initiated before the finalization of regulatory financial statements based on historical accounting costs.



Step 1 should stipulate the requirements to prepare and produce costs in a prescribed format, i.e. regulatory financial statements and accounts based on historical costs. The format should at a minimum separate operating costs and capital costs into network and retail business accounts and require a transparent system of transfer prices in accordance with section 6.2¹¹.

Step 2 should refine the calculations and outputs produced in Step 1, where non-relevant costs are excluded from the cost basis for calculating wholesale rates. Such non-relevant costs should normally include retail related costs for sales, marketing and billing.

Step 3 should re-valuate all assets into current costs based on their replacement cost. The current cost evaluation should work as a proxy for forward looking costs. The result should be regulatory financial statements based on current cost valuations, and the exclusion of costs determined to be non-relevant to the provision of the wholesale products.

Step 4 should imply the preparation and production of statements based on a LRAIC model. The model should take into account the need for a mark-up of joint and common costs to the long run incremental cost of a specific wholesale product, i.e. LRAIC plus a mark-up. For simplicity the mark-up should be equal and proportionate.

The main approach for calculating LRAIC based prices should be a top-down model, i.e. the actual costs of an operator but adjusted for forward looking valuations and taking into account possible levels of inefficiencies. The top-down approach may be combined with a bottom-up engineering model approach, which would calculate the incremental

¹¹ Bottom-up modeling and/or benchmarking may be used where the historical accounts of an operator provide an inadequate basis for cost oriented pricing.

costs based on the equipment and activities required in an efficient network operation.

6.2 Accounting Separation and Transfer Prices

Operators with significant market power should be required to prepare a system of accounting separation with transparent and non-discriminatory transfer prices between, at a minimum, its network and retail business, and wholesale transfer prices towards other external operators.

For fixed incumbent operators the network business should be separated into an access business and a core network business¹².

The access business should cover of all subscriber lines/connections to the network. This will include those components of the network which are not traffic sensitive and are dedicated to a particular customer including the local loops and the line cards and ports located at concentrators and/or exchanges.

The core network business should the provision of interconnection services (i.e. internally to the retail business and externally to other operators, transit services and carrier's carrier services.

The cost allocation principles and attribution methods applied should be based on generally accepted costing principles, i.e. cost causality, objectivity, consistency and transparency, whereby revenues, operating costs, assets and liabilities should allocated to the different business segments.

The attribution methods proposed by the operator should have to be approved by the regulator before being applied.

The regulatory financial statements and accounts prepared in accordance with the regulator's requirements should be supported by an independent external audit.

¹² For mobile operators a separation of the network business into further "sub-businesses" is not applicable.

7 Procedures

7.1 Publication Requirements

Standard agreements and offers on wholesale pricing arrangements by operators should be made publicly available, at the regulatory Authorities' discretion¹³.

Operators with significant market power should be required to publish standard prices for access to and use of its network, which should include showing that the offers on wholesale products and services are on the same terms and conditions as those offered to itself or to any other subsidiary, affiliate, or any other party to which the interconnection products are provided.

Authorities should keep procedures and processes transparent which should normally involve to publishing its decisions, including the reasons for the decisions.

SADC Member States should ensure that specific obligations imposed on operators are published and that specific product and geographical markets are identified.

The Authority's analysis and determination of relevant markets should be consulted with the industry and be publicly available.

7.2 Dispute Resolution

In resolving disputes, the national Authority should primarily take into account:

- (a) the user interests;
- (b) the promotion of fair competition; and, where appropriate,
- (c) the availability of technically and commercially viable alternatives to the services or facilities requested.

At the request of either party, the Authorities should issue a decision within the prescribed time period in accordance with the relevant legislation, or in the absence of such, within the shortest time period available, but sufficient to allow fair consideration of disputed facts¹⁴.

¹³ An exception may be made with regard to sections that deal with the parties' specific expansion plans for coverage of networks and services, and customer penetration. At the regulator's discretion such sections, and potentially other related areas, may be classified as commercially sensitive information, and therefore treated as confidential.

¹⁴ Authorities may need to make quick determinations, which may not be based on detailed investigations, where such determination is critical to the viability of one or

Authorities should ensure that procedures are fair, transparent and clearly established well in advance.

7.3 Enforcement and Penalties

The Authority should have necessary powers and tools to effectively enforce its determinations and decisions.

When an Authority has proposed to make a decision there should be:

- (a) a written statement explaining the matters to which the objection has been made;
- (b) the actions and remedies that are proposed; and
- (c) the reasons therefore.

The party or parties receiving the statement should normally have the opportunity to make representations.

Where the Authority makes a decision to the party involved, it will be required to comply with the decision. It may include a direction to modify or terminate an agreement in question.

If an operator fails to comply with the direction, the Authorities may impose necessary penalties.

he penalties for excessive and anti-competitive wholesale prices should be substantial and be determined based on actual or expected harm of the pricing behavior.

The penalties may be determined in relation to the turnover of the party that abuses its market power. Financial penalties up to a specified maximum percentage of an individual operator's annual turnover may be enforced. Such annual penalty may apply for a specified period, if the anti-competitive pricing conduct continues.

more providers in the sector. There should be a possibility to later amend such determination when a more detailed investigation has been finalized. There should also be a stipulated time limit and deadline for the finalization of such investigations. The time required will vary depending on the complexity of the issues involved.

8 CONCLUSIONS

The time target set for the implementation of the policy guidelines and the regulations should be within twelve months after the adoption date by the SADC Ministers responsible for Communications¹⁵.

Implementation should be understood to mean the adoption and public communication of the policy and regulations in the individual SADC Member State.

The implementation of the policy guidelines and regulations on wholesale pricing have to be integrated and harmonized with other major activities carried out in the individual SADC Member States such as the implementation of other adopted guidelines.

SADC Member States should be required to report on the progress of the implementation of the policy and regulations on wholesale pricing.

The national sector regulator, where relevant in co-operation with other authorities, should be responsible for reporting to the TRASA Secretariat every three months on the progress of all relevant policy guidelines and regulations.

The TRASA Secretariat should be responsible for compiling the information and report on the progress to the SADC/SATCC Committee.

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End//.....

¹⁵ Some countries are in a better position to quickly implement the policy, whereas others may raise concerns on potential conflicts with their own national policies and regulations. There may in the latter case be a justification to deviate from the time target.

