ESA | EFTA Surveillance Authority

Brussels, 22 April 2021
Case No: 86639
Document No: 1193192

Póst- og Fjarskiptastofnun
Sudurlandsbraut 4
108 Reykjavik
Iceland

For the attention of:
Mr Hrafnkell V. Gíslason
Managing Director

Dear Mr Gíslason,

Subject: Review of Míla's wholesale tariffs in the market for trunk segments of leased lines in Iceland - Remedies

Comments pursuant to Article 7(3) of Directive 2002/21/EC (Framework Directive)[1]

I. PROCEDURE

On 26 March 2021, the EFTA Surveillance Authority ("the Authority") received a notification of a draft national measure in the field of electronic communications pursuant to Article 7 of the Framework Directive from the Icelandic national regulatory authority, *Póst- og Fjarskiptastofnun* ("the PTA"). It concerns the imposition of remedies in the market for wholesale trunk segments of leased lines in Iceland.[2]

The notification became effective on the same day.

National consultation was carried out, pursuant to Article 6 of the Framework Directive, during the period from 29 October 2020 to 13 November 2020.

The period for consultation with the Authority and the national regulatory authorities ("NRAs") in the EEA States, pursuant to Article 7 of the Framework Directive, expires on 26 April 2021.

[1] Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communications networks and services, OJ L 108, 24.4.2002, p. 33 (as amended by Regulation (EC) No 717/2007, OJ L 171, 29.6.2007, p. 32 and Regulation (EC) No 544/2009, OJ L 167, 29.6.2009, p. 12), as referred to at point 5 cl of Annex XI to the EEA Agreement and as adapted to the Agreement by Protocol 1 ("the Framework Directive").

[2] Corresponding to market 14 of the EFTA Surveillance Authority Recommendation of 14 July 2004 on relevant product and service markets within the electronic communications sector susceptible to *ex ante* regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communication networks and services, as incorporated into the Agreement on the Economic European Area (No 194/04/COL) ("the 2004 Recommendation").

Pursuant to Article 7(3) of the Framework Directive, the Authority and the EEA NRAs may make comments on notified draft measures to the NRA concerned.

II. DESCRIPTION OF THE DRAFT MEASURE

II.1. Background

In its Decision No. 21/2015[3] the PTA designated Míla ehf. ("Míla") with significant market power ("SMP") in the wholesale market for trunk segments of leased lines. Furthermore, the PTA imposed obligations on Míla regarding access, non-discrimination, transparency (publication of a reference offer), price control, cost accounting and accounting separation. In particular, the PTA required Míla to prepare a cost model for the calculation of the wholesale prices for trunk segments of leased lines based on fully-allocated historical costs ("FAC HCA").[4]

In parallel, the PTA notified cost analyses and resulting wholesale tariffs for trunk segments of leased lines, Ethernet services, Metropolitan Data Highway ("MDH") and temporary connections.[5] In November 2015, the PTA also notified a recalculation of the wholesale tariffs for MDH connections.[6] Míla was further required to review these tariffs no later than by the end of 2016 and on an annual basis thereafter, subject to authorisation by the PTA (following national consultation and consultation with the Authority).

In April 2018,[7] the PTA notified a draft decision, which concerned a review of wholesale tariffs for leased lines, MDH, Ethernet service ("MPLS-TP") and Sync-Ethernet – a new service offered by Míla.

Subsequently, in October 2019,[8] the PTA submitted to the Authority a draft decision notifying a minor change in Míla's tariff, following the introduction by Míla of an additional location for offering 100 Gb/s MDH.

In its assessment of the above draft measures, the Authority commented *inter alia* on the need to ensure a prompt and timely implementation of the proposed obligations.

II.2. Current notification

The currently notified draft decision concerns a review of Míla's tariffs and results from obligations imposed on the company by PTA Decision No. 21/2015.

Míla submitted a cost analysis to the PTA based on the same methodology as in previous analyses and taking account of data from the operational year 2018. The initial cost analysis was submitted to the PTA in October 2019 with further revisions submitted in January 2020. In February 2020, Míla submitted a cost model for 100 Gb/s on the fibre-optic ring.

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[3] Notified to the Authority on 1 July 2015, Case 77596.
[4] In its reply to the Authority's RFI, the PTA explained that it intended to review the costing methodology in the next market analysis, if the result of that analysis still showed a position of SMP on the market. The frequency and the method of the tariff reviews would also be reconsidered at that time.
[5] Notified to the Authority on 1 July 2015, Case 77597.
[6] Notified to the Authority on 23 November 2015, Case 78301.
[7] Notified to the Authority on 17 April 2018, Case 82013.
[8] Notified to the Authority on 16 October 2019, Case 84271.

The price control set by the PTA will allow Míla to increase monthly charges in the trunk line market by 2.59% with respect to the previous year. The increase does not cover one-off charges, monthly charges for Sync-Ethernet and for ports and special agreements.

In its calculations, the PTA allows for a 6.9% weighted average cost of capital ("WACC") for the year 2018. In this context, the PTA refers to the European Commission Notice of 6 November 2019 on the calculation of the cost of capital for legacy infrastructure ("the Notice"). The PTA considers that the current draft decision falls under the Notice's transitional period mentioned in recital 71. However, the PTA has indicated that it will follow the Notice more closely at the next price review, expected in 2022.

The PTA considers it appropriate that in the next revision of the tariffs in this market, the cost model will be reviewed in its entirety. Míla shall submit a revised cost model to the PTA no later than 1 April 2022. The cost model shall be in accordance with the criteria set out in PTA's Decision No. 21/2015, dated 12 August 2015.

Furthermore, the PTA has commenced the analysis of the market for trunk segments of leased lines and it expects to conclude that analysis later this year or next year.

III. COMMENTS

The Authority has examined the notified draft measure and has the following comments:

Timely analysis and notification of next market reviews

The PTA's market review decision for market 14/2004 dates back to 2015. The Authority notes further that the PTA expects to finalize its next review later in 2021 or in 2022, implying a delay of six to seven years in the review cycle for this market. It is imperative that NRAs undertake market reviews at regular intervals to ensure that any decisions to impose, maintain, amend or withdraw obligations, as foreseen in Article 16(2) of the Framework Directive, are taken on the basis of up-to-date and relevant market analyses. The Authority therefore urges the PTA to finalize its next full market analysis without undue delay, in line with the PTA's obligations under the EEA regulatory framework.

Estimating the WACC in accordance with the European Commission's Notice

The Authority agrees with the PTA that the current draft decision falls within the transitional period in recital 71 of the Notice and acknowledges the PTA's intention to follow the Notice more closely at the next price control review. In particular, there seem to be disparities in the calculation of the risk-free rate and the equity risk premium. The Authority invites the PTA to ensure that its WACC methodology is in line with the approach recommended by the Commission and that any departure from it is duly justified in future price controls. In this regard, the Authority would also like to point out that recital 70 of the Notice indicates that it is appropriate to update the WACC value at least once per year to take account of recent economic conditions.

Need to ensure that prices reflect efficient costs

In order to assess the tariffs for trunk segments, the PTA uses a top-down cost model developed by Míla and based on fully-allocated costs and historical cost accounting ("FAC HCA"). Although less complex than bottom-up models, top-down cost models based on accounting data run the risk of diverging from efficiently incurred costs. In this regard, the PTA has indicated that total trunk capacity has increased considerably (given that the growth in Ethernet service volumes has more than compensated for a slight decline in traditional leased lines over the period 2016-2018). In spite of this volume increase, which should result in increasing economies of scale, the cost model developed by Míla estimates, somewhat counterintuitively, increased costs supporting an increase of 2.59% in all service tariffs. For this reason, the Authority invites the PTA to ensure that in the next revision of the cost model the cost estimates used by Míla reflect efficiently incurred costs. In that regard, the Authority invites the PTA to assess whether the level of prices and their trends follow a pattern consistent with that in other EEA countries.

IV. FINAL REMARKS

On a procedural note, the Authority recalls that any future amendments to, or more detailed implementation of, the draft remedies consulted on in the current notification will require re-notification in accordance with Article 7(3) of the Framework Directive.

Pursuant to Article 7(5) of the Framework Directive, the PTA shall take the utmost account of comments of other regulatory authorities and the Authority. It may adopt the resulting draft measure and, when it does so, shall communicate it to the Authority.

The Authority's position on the current notification is without prejudice to any position the Authority may take in respect of other notified draft measures.

Pursuant to Point 15 of the Procedural Recommendation,[9] the Authority will publish this document on its eCOM Online Notification Registry. The Authority does not consider the information contained herein to be confidential. You are invited to inform the Authority within three working days[10] following receipt of this letter if you consider, in accordance with EEA and national rules on confidentiality, that this letter contains confidential information which you wish to have deleted prior to publication. You should give reasons for any such request.

Yours sincerely,

Gabrielle Somers	Emily O'Reilly
Deputy Director	Deputy Director for Competition
Internal Market Affairs Directorate	Competition and State Aid Directorate

This document has been electronically authenticated by Emily OReilly, Gabrielle Somers.

[9] EFTA Surveillance Authority Recommendation of 2 December 2009 on notifications, time limits and consultations provided for in Article 7 of the Act referred to at point 5cl of Annex XI to the Agreement on the European Economic Area (Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services), as adapted by Protocol 1 thereto, OJ C 302, 13.10.2011, p. 12, and available on the Authority's website at http://www.eftasurv.int/media/internal-market/recommendation.pdf ("the Procedural Recommendation").

[10] The request should be submitted through the eCOM Registry, marked for the attention of the eCOM Task Force.