ITU GSR-21 Regional Regulatory Roundtable and Regional Economic Dialogue for CIS countries (RRR-RED CIS-21)

Региональный регуляторный круглый стол в рамках ГСР-21 и Региональный экономический диалог для стран СНГ (РРК-РЭД СНГ 2021)
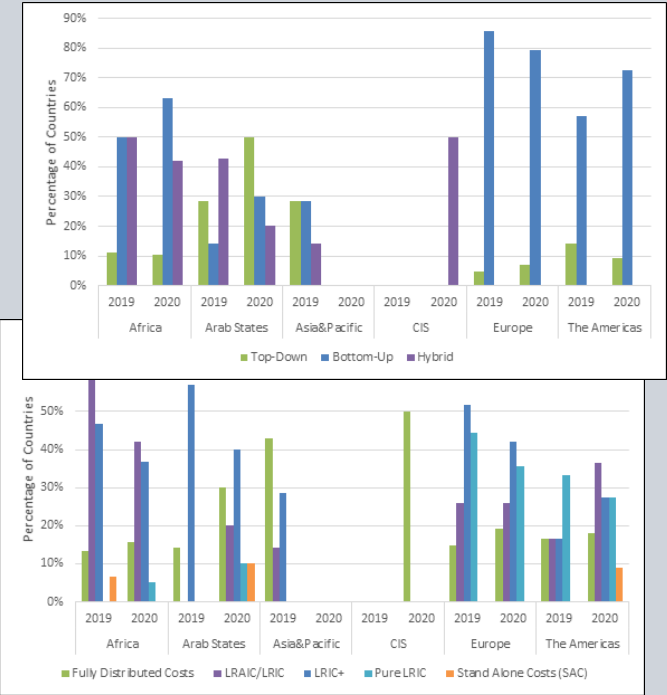
Virtual meeting | 15-16 June 2021, 9:00 – 12:00 (+3 GMT)

Advances in regulatory costing and pricing strategies in the digital era

Jorge Martínez Morando,
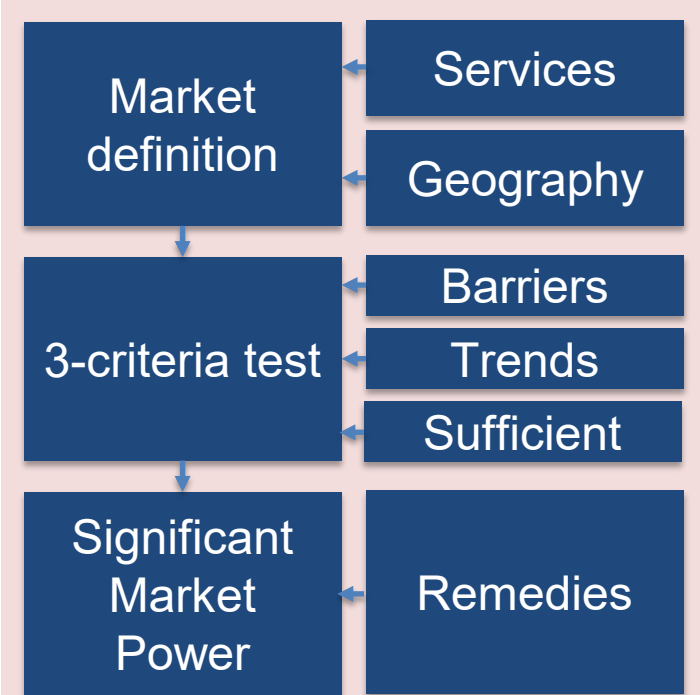Partner at Axon Partners Group and
Vice-rapporteur for ITU-D Q4/1

As part of ITU-D Q4/1 mandate, we analysed the pricing methodologies applied around the world

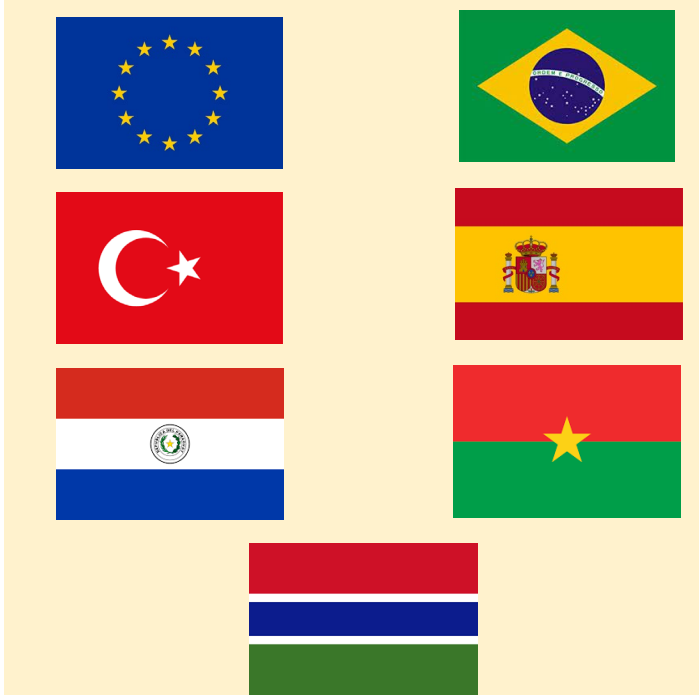## Costing methodologies

Market analysis

Market definition ← Services

Market definition ← Geography

3-criteria test ← Barriers

3-criteria test ← Trends

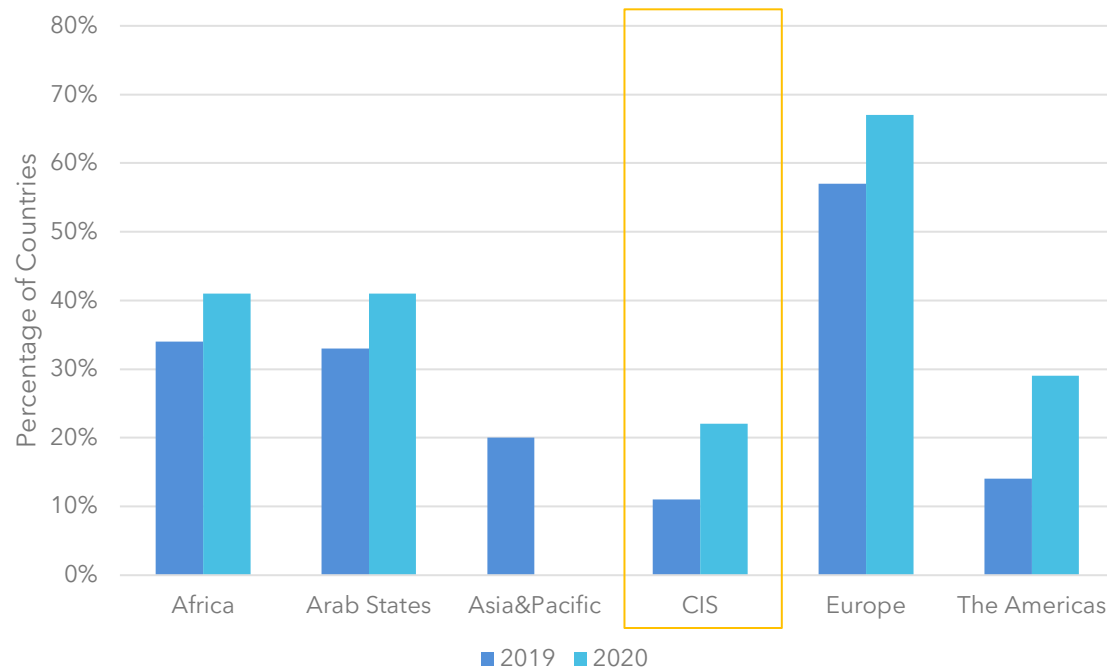3-criteria test ← Sufficient

Significant Market Power ← Remedies

Use cases

Even if it grew on 2020, we observed a lower adoption of cost modelling for advanced services in CIS region vs the rest of the world
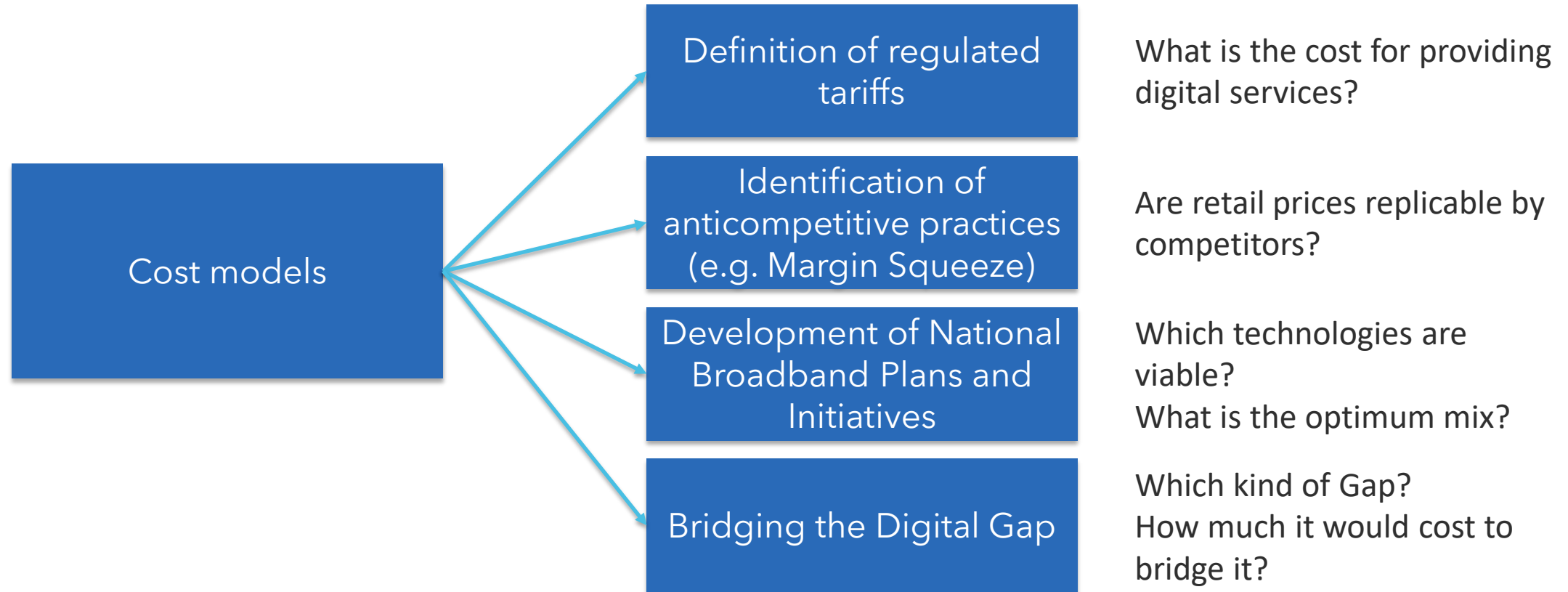
Reported modelling for fixed advanced wholesale services*

Reported modelling for mobile advanced wholesale services*

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Note (*): Advanced wholesale services mean services based on NGN/IP networks
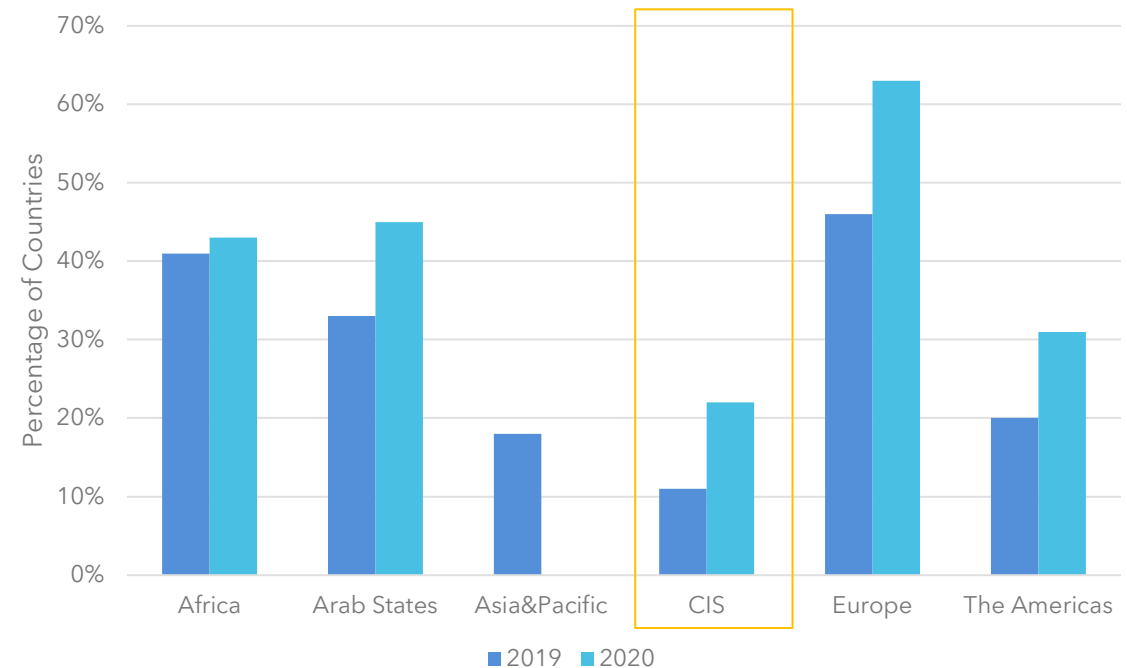
But, for what are cost models developed? They support decision making on several regulatory and public policy aspects

Cost models

→ **Definition of regulated tariffs**

What is the cost for providing digital services?

→ **Identification of anticompetitive practices (e.g. Margin Squeeze)**

Are retail prices replicable by competitors?

→ **Development of National Broadband Plans and Initiatives**

Which technologies are viable?
What is the optimum mix?

→ **Bridging the Digital Gap**

Which kind of Gap?
How much it would cost to bridge it?

In order to support the NRAs to develop cost models, from Q4/1 we have produced the "Guidelines on Cost Modelling"

❖ ITU published in 2009 its <u>Regulatory Accounting Guide</u>

❖ This document provides an overview of cost modelling topics, but does not enter into much detail about relevant technical methodological aspects

❖ With the <u>Guidelines on Cost Modelling</u> we provide more level of detail that will be useful for implementing cost models, especially for NRAs.

The first decision when developing a cost model is the general modelling approach

Starting point?

Real costs of the company

Top-down

Objective?

Knowing services' revenues, costs and margins

Regulatory Accounting

Identify cross-subsidies between company divisions

Accounting Separation

Demand, geographic info, processes, equipment...

Bottom-up

Objective?

Identify margin squeeze cases

Margin* Squeeze Model

Calculate services' costs, sensitivity analysis, forecast

Cost Model

Note (*): These kind of models are not discussed in the Guidelines, being their problematic more about regulation that modelling issues.

Once the approach is selected, it is important to define several methodological aspects

Relevant topics and options			Bottom-Up	Top-Down
Cost Standard ▸ Fully Distributed (FAC/FDC)	▸ Pure Incremental (LRIC)	▸ Incremental+ (LRIC+)	✓	✓
Cost elements to consider ▸ Network ▸ Licenses and spectrum	▸ Retail ▸ General and Admin.	▸ Cost of Capital	✓	✓
Treatment of capital ▸ Assets valuation	▸ Modern Equivalent Assets	▸ Annualisation method	✓	✓
Treatment of revenues ▸ Financial information and granularity	▸ Treatment of bundles		–	✓
Reference operator ▸ Real Operators	▸ Hypothetical operator	▸ Hypothetical new entrant	✓	–
Services and increments ▸ Services to include	▸ Definition of increments (only for LRIC/LRIC+)		✓	✓
Geographical modelling ▸ Geotypes definition	▸ Modelling based the information available		✓	–
Network topology design ▸ Scorched node	▸ Modified Scorched Node	▸ Scorched earth	✓	–

Legend: ✓ Applicable   – Not applicable

Note: All these aspects are described in detail in the Guidelines

The guidelines provide also advice regarding how to structure a cost modelling project

Bottom-up

1. Kick-off | 2. Methodology | 3. Consultation on Methodology | 4. Data gathering | 5. Data validation | 6. Model development | 7. Consultation on the Model | 8. Regulatory decision

Top-down

1. Regulatory framework definition | 2. Development of implementation manual | 3. Model implementation | 4. Audit/revision

Note: All these aspects are described in detail in the Guidelines

Thank you very much

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