

**ANALYSYS MASON questions to EY:**

**1. Compliance of GNCC Decision on MVNO access regulation with EU ex-ante regulatory Framework**

As we (Analysys Mason) have already stated at the meeting we have reviewed GNCC decision on MVNO access regulation in details and our conclusion is that market definition, market analysis and SMP assessment presented in the GNCC decision is not in line with European Union Framework on ex-ante regulation; Our full report will be available by the end of the week;

Your (EY) answer on our (Analysys Mason) question (how EY has examined compliance of GNCC's decision with European Union regulatory framework – i.e. has EY only checked if headings of general regulatory steps (like market definition/market analysis/SMP assessment) are written in the GNCC document or has EY analyzed GNCC decision in details?) was that EY has not analyzed GNCC decision in details;

To avoid misunderstanding, please confirm once more in written form that EY has not examined compliance of GNCC's decision with European Union regulatory framework in details and that EY has only checked if general regulatory steps (like market definition/market analysis/SMP assessment) are written in the GNCC document?

**Answer:** COMCOM Decision is in line with EU regulatory framework. Under the **Commission Recommendation of 11 February 2003 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** , Commission determined 18 markets (11 wholesale and 7 retail markets) susceptible to ex ante regulation. The reason, why ex ante regulated markets was shortened by the time of Recommendation of 17 December, 2007 was the development on competitive environments on relevant markets and the telecommunications services itself. The remaining markets have been identified on the basis of three cumulative criteria and a national regulatory authority may choose not to carry out the market analysis procedure. For the markets (11 Markets), which are in the Recommendation *2003/311/EC* and are not in recommendation *2007/879/EC*, national regulatory authorities should **have the power** to apply the three-criteria test in order to assess whether, on the basis of national circumstances, a market is still susceptible to ex ante regulation. Regulatory authorities should ensure that the following three criteria are cumulatively met:

- (a) the presence of high and non-transitory barriers to entry. These may be of a structural, legal or regulatory nature;
- (b) a market structure which does not tend towards effective competition within the relevant time horizon. The application of this criterion involves examining the state of competition behind the barriers to entry;

(c) the insufficiency of competition law alone to adequately address the market failure(s) concerned.

Although the Commission removed the wholesale mobile access and call origination market (market 15 in the 2003 version of the European Commission's recommendation) from the list of relevant markets already in 2007, it still remained subject to ex ante regulation in three EU/EEA member states: Cyprus, Norway and Spain (deregulated in 2017).

Nkom defined a relevant national wholesale market that includes access by national roaming; MVNO access; and service provider access. As the mobile access and call origination market is no longer included in the Commission recommendation on relevant markets, Nkom had to assess whether the market still satisfies the three cumulative criteria for ex ante regulation.

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Also, it is important to highlight, that under the recital 145 of the DIRECTIVE (EU) 2018/1972 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 11 December 2018 establishing the European Electronic Communications Code (EECC), National regulatory authorities should define relevant geographic markets within their territory taking into utmost account the Commission Recommendation on relevant product and service markets (the 'Recommendation') adopted pursuant to this Directive and taking into account national and local circumstances. Therefore, national regulatory authorities should at least analyze the markets that are contained in the Recommendation, including those markets that are listed but no longer regulated in the specific national or local context. National regulatory authorities should also analyze markets that are not contained in that Recommendation, but that are regulated within the territory of their jurisdiction on the basis of previous market analyses, or other markets, if they have sufficient grounds to consider that the three criteria provided in this Directive are met.

## **2. Remedies (obligations) imposed by GNCC to support fair competition on the market- compliance with EU framework.**

We are fully aware that EY recognizes that according to the European Union regulatory framework if ex-ante intervention and presence of SMP(s) on the relevant market is not justified by the regulatory authority, remedies (obligations) should not be imposed at all;

Based on your answer (that you have not analyzed GNCC decision in details), our (Analysys Mason) questions are as follow:

- a) Does it mean that you have not examined whether or not ex-ante intervention and presence of SMP(s) on relevant market is justified by GNCC in its market analysis document (decision) and
- b) If such how could you arrive to the conclusion (Slide 18) that "GNCC followed EU regulatory approach" by "imposing remedies required to support fair competition on the market"?

**Answer:** As stated in Report (p. 18) EY reviewed general steps taken by GNCC to liberalize telecommunications market in Georgia by MVNO access and they are in line with EU regulation framework. GNCC followed EU regulatory approach by defining respective market, designating SMPs and imposing the list of remedies required to support fair competition on telecommunications market.

### 3. Retail Prices

We note that you have assumed that MVNO introduction should lead to no decrease in ARPU or retail prices and one of the reasons is that “**current retail price margins allow very limited possibility to decrease prices below current levels**”. On the other side, in GNCC’s decision, a price decrease is described as the regulatory objective.

Don’t you think that current price levels are one of the indications that Georgian Mobile retail market is sufficiently competitive?

**Answer:** Average Price level cannot be the only indicator for sufficient competition in mobile retail market, NRA has different tools to evaluate competition e.g., HHI index.

### 4. MVNO impact - Key modeling assumptions

- a) Why do you assess performance on EBIT level rather than FCF? Cost of capital is estimated at 14.95% pre-tax for mobile operators in Georgia, around twice the average WACC of mobile operators in the EU.
- b) How do you assess the performance of the total market without assessing the performance of each operator separately? Is there a chance that one or even two operators are pushed out of the market due to negative FCF?

**Answers:**

- a) To evaluate MVNO introduction on existing MNOs EY used information from accounting separation statements. There were discussed two scenarios and it was assumed that MVNO Introduction will not cause price erosion, therefore effect on EBIT and FCF would be same.
- b) Scope of the work was to evaluate impact on whole market, not separate entities.

**Additional questions**

## 5. EBIT/FX

a) What is the source of the EBIT margin of 46%? The reason we are asking this question is that Silknet's mobile segment EBIT margin is around 25%, Veon which is mobile only player is 25% (these are audited numbers), to arrive to 46% for total market Magticom should be up to 80%, which is very unlikely since EBIT cannot be higher than EBITDA? How do you arrive to 46%?

	Magti	Silknet	VEON	Total
Revenue	337,121	208,342	111,519	656,982
EBIT	235,507	31,388	27,425	294,320
EBIT %	70%	15%	25%	45%

b) Please provide the source of EBITDA and explain how you have calculated EBITDA

### *Answers:*

- a) Based on the information provided by COMCOM average EBIT Margin for 2019 year is 45%.
- b) EBITDA was calculated based on accounting separation documents provided by Operators to COMCOM.
- c) Largest part of the MNOs CAPEX and sizeable part of the OPEX are foreign currency denominated, which is explained by the fact that Georgian telecom's ability to negotiate local currency contracts with international vendors like Ericsson, Huawei, Cisco, etc. is very limited. Your conclusion that MNO "**current retail price margins allow very limited possibility to decrease prices below current levels**" is based on accounting separation document. The latest accounting separation document has been prepared for 2019 when the average exchange rate was 2.8. Today it is 3.3, 18% higher, which apparently further distressed MNOs profitability. Do you consider that impact in the model or do you assume constant currency starting from 2019?

### *Answer:*

- c) Network cost, depreciation, sales and customer care and general administrative costs – are the fixed cost not changing during the period of analysis. (p. 47) Increase of exchange rate was not considered.

## DENTONS questions to EY:

### 6. Abuse of dominance by MNOs on retail market

The executive summary of your report, under the MVNO Access Obligation Background, stipulates that "according to GNCC market analysis, above market conditions allowed **SMPs to abuse the dominance on retail market**" and that "**this antitrust behavior by SMPs was observed** after deregulation of retail price caps when GNCC had to perform mobile retail market analysis, to **identify**

**the abuse of dominance by SMP's** and to impose the remedies in June 2020". As far as we are aware neither the GNCC, nor the competition authority or a Georgian court, has ever established an abuse of dominant market power by MNOs on the retail market or commenced administrative proceedings to that effect.

- a) What evidence does your statement rely on when stating that SMPs abused the dominance on the retail market? You will probably agree that when you are making such allegations they should be based on facts;

**Answer:** "Dominance" - wording was respectively updated in the Report.

## 7. **Cyber-security**

One of the main concerns of MNOs in relation to introduction of MVNO access is increased risks of information-cyber-security. In this context you referred to the Law of Georgia on Personal Data Protection But we don't see why the personal data protection law is relevant in terms of analyzing the risks of cyber-security.

We would expect you to analyze and assess information security measures under the Law of Georgia on Information Security and draft law which proposes to extend the application of the law to certain Telco companies.

- a) Do you believe that the Personal Data Protection Law regulates the measures MNO or MVNO should take in order to protect integrity and safety of its information system or protect its information system from cyber-attacks?
- b) And why you have ignored draft Georgian law on Information Security?

**Answer:** Georgian legislation related to data protection and information security is in line with EU framework and the integrity and safety of information system are protected.

## 8. **Measures to prevent unfair cross-subsidy**

### a. **Law on Competition**

We understand from your report that the main legal mechanism which you consider to be a tool to prevent potential cross subsidies by Banks or Bank affiliates to telecom is the Law of Georgia on Competition and in particular its articles 6 and 7. Having analyzed the above articles and your report, we came to conclusion that the Law of Georgia on Competition may not be effective to prevent potential cross-subsidies by the banks or bank affiliates to the telecom sector because:

- (1) on the one hand, both Articles 6 and 7 are ex-post regulations allowing for regulatory intervention only after the breach of law has already occurred; and
- (2) On the other hand, article 7 does not apply to similar cases of cross-subsidization at all. This means that the only potentially applicable provision is Article 6 which restricts abuse of power by dominant undertakings on the relevant market. The initial and important criterion for

establishing dominant power on the relevant market is the market share of the undertaking. Under the law there is a presumption that generally an undertaking holding 40% or less on the relevant market is not considered as dominant undertaking.

Considering the above analysis:

Why do you think that article 6 is going to be effective to prevent the possibility of cross-subsidization in our scenario?

**Answer:** Based on the review of respective legislations and competencies of respective agencies, EY conclude that cases related to the unfair competition will be regulated and addressed by Competition Agency of Georgia as well as sector regulatory bodies of telecom and banking (COMCOM & NBG)

Potential cross-subsidy and other abuse of market power between sectors (e.g. telecom & financial, including with affiliated companies) are regulated by the Competition Law of Georgia and NBG regulations s described on pages 22 & 24 of the report.

#### **b. Banking Regulations**

We note your conclusion in the report stating that “due to the fact that the competition-related norms given in the Law on Commercial Banks are not very precise, the possibility for the commercial banks to abuse the significant market power and create artificial barriers for the entrants may actually exist.” Your own assessment leads us to conclude that the regulations in the banking sector are not sufficient to address competition law problems in the banking sector itself, not to say the potential problems with the banks abusing their power in other sectors.

On another hand your report refers to Article 22 of the Law on Commercial Banks, Code of Ethics for Commercial Banks and the Rules of Management of Conflict of Interest for Commercial Banks, and lists them as tools preventing potential cross-subsidies by banks on telco market.

Having reviewed these normative acts we understand that (1) first, none of these legal acts expressly restrict the banks to cross-subsidize prices; and (2) second, all of these legal acts apply only to banks and not to their affiliates. The Conflict of interest rules for banks, which essentially requires the banks to conduct transactions with their related parties on an arms length basis, applies to banks’ dealings vis a vis its related parties.

Having this in mind, could you please explain

- a) if and to what extent the above mentioned banking regulations restrict a bank’s/or bank affiliates’ ability to package their/or their partner MVNO’s telecom services with banking or other products and offer to customers at discounted (or without discounted) prices as part of the package; and
- b) Do any of these regulations restrict the activities of the banks’ affiliates?

*Answer:* The Scope for EY was to ensure that there are sufficient instruments to prevent market moves, that will harm telecom market from misconducts such as cross-subsidization. Reviewing above mentioned regulations, we can assume that Banks can not directly enter and cannot cross-subsidize their affiliates in telecom market.

**c. Telecommunications**

According to your report the Law on Electronic Communications includes a restriction related to subsidization and you also noted that “this provision refers to the activities of SMPs.” We fully agree that the restriction on cross-subsidization imposed by the GNCC as part of ex ante regulation applies only to SMPs. So GNCC will not be able to impose on MVNOs the restriction on cross subsidization without conducting market analysis and establishing significant market power of such MVNOs. Under the law the initial criteria of defining SMP is market share which should be at least 40% for single SMP and at least 80% in case of three operators.

Your report also stipulates that “based on international experience, MVNOs gain on average less than 7% of the market”, maximum MVNO market share observed in EU was 28%.

Given the above, do you think it is realistic that MVNOs would be subject to SMP obligation relating to subsidization restriction?

*Answer:* Based on EU practice obligation related to cross-subsidization are used for vertically integrated undertakings, in certain circumstances, MVNOs may be subject to accounting separation obligation, thus MVNOs will rather be subject to ex-post regulation through Margin Squeeze.

**Other remarks and notes:**

9. The executive summary of your report, under the MVNO Access Obligation Background, stipulates that “This antitrust behavior by SMPs was observed **after deregulation of retail price caps, when GNCC had to perform mobile retail market analysis,**”; this fact is not correct and please recheck; in addition our comment regarding “**abusing by SMPs the dominance on retail market**” is given in question 6 above;

*Answer:* Rephrased, no more “Abusing” term is used (p. 5).

10. We (Analysys Mason) have identified some approximations and mistakes in EY report:  
The market of access and call origination on public mobile telephone networks (Market 15/2003, that included MVNO access) disappeared from the European Commission Recommendation of relevant markets susceptible to ex-ante regulation as early as the second iteration of this Recommendation, in 2007, and not the third iteration, in 2014.

*Answer:* Agreed. Added respective clarification (p. 14).

- In the Netherlands, Market 15/2003 has never been regulated under the European regulatory framework.t7\*\_\*

**Answer:** According to some of the reports which are in possession of EY, the national roaming was regulated in Netherlands before 2003. However due to lack of source documentation from AMC, we agree to remove Netherlands from the list – removed (p. 14).

- In Denmark, although a law regulated MVNO access before the European regulatory framework was established, Market 15/2003 has never been regulated under the European regulatory framework.
- In Ireland, although the regulator initially regulated Market 15/2003 under the European regulatory framework, this decision was then annulled by the appeal body.

**Answer:** ComReg found Vodafone and O2 to be jointly dominant in M15/2003 and obliged them to meet reasonable requests for access, including MVNO access (ComReg decision of 24 March 2005). However, in Dec. 2005, an appeal panel annulled the SMP designation, and the remedies imposed by ComReg in M15/2003 Denmark and Ireland Removed from the list on (PG 14). Slovenia, Slovakia, Cyprus, Spain, Malta and Norway (associated) designated SMP on Market 15 since the Commission Recommendation of 11 February 2003:

[https://www.cullen-international.com/client/site/documents/B5TEEU20140047\\_1e341ae7-5da7-4c46-ac13-18ae63eab661](https://www.cullen-international.com/client/site/documents/B5TEEU20140047_1e341ae7-5da7-4c46-ac13-18ae63eab661)

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