This is an unofficial translation. The legally binding text is the original Czech version.

Czech Telecommunication Office
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[*Stamp and Signature*:
THIS DECISION BECAME FINAL
on *[handwritten]* *2. 5. 2006*
Czech Telecommunication Office
Economic Regulation Department
Date *[handwritten]* *2. 5. 2006* *[signature:Smrkovská]*]

Prague, 26 April 2006
Ref.: 15 843/2006-611/IV.vyř.

In proceedings initiated *ex officio* with ČESKÝ TELECOM, a.s. with registered office at Olšanská 55/5, 130 34 Prague 3, Reg. Number 60193336 on 16 March 2006 in the matter of the imposition of obligation related to price regulation on an undertaking with significant market power, the Council of the Czech Telecommunication Office as the appropriate state administration body under Section 107(8)(b)(5) of Act No. 127/2005 on Electronic Communications and on Amendment to Certain Related Acts (Electronic Communications Act), as amended (the "Act") and under Section 10 of Act No. 500/2004, Rules of Administrative Procedure, as amended, hereby issues this

Decision on Price No. CEN/9/04.2006-18:

I.

(1) Under Section 51(3)(g) and Section 59 of the Act and in accordance with the results of the analysis of the relevant market of "Call Termination in Individual Public Telephone Networks at a Fixed Location", issued in Czech Telecommunication Office's Measure of General Nature No. A/9/04.2006-19, the obligation to negotiate charges for interconnection in its public telephone network for the call termination service (hereinafter referred to as "termination prices") is hereby imposed on ČESKÝ TELECOM, a.s., with registered office at Olšanská 55/5, 130 34 Prague 3, Reg. Number 60193336 (hereinafter referred to as the "Party to the Proceedings") so as to avoid exceeding the maximum prices specified below:

Termination with interconnection at:	Traffic time	Maximum termination price [CZK/min] excl. of VAT
a) local switch (HOST)	peak	0.30
	off peak	0.15
b) last transit switch	peak	0.38
	off peak	0.19

a) termination with interconnection at local switch means a case where the end point in the interconnected publicly accessible telephone network to which the call is routed is located in the access area of the gateway switch in which the networks are interconnected, the gateway switch being the local switch;
b) termination with interconnection at the last transit switch means a case where the end point in the interconnected publicly accessible telephone network to which the call is routed is located in the access area of the gateway switch in which the networks are interconnected, the gateway switch being the transit switch.

The peak time is the period from 7:00 to 19:00 hours on workdays. The off peak time is the period from 19:00 to 7:00 hours of the following day on workdays and the entire 24 hour period on Saturdays, Sundays and on holidays recognised by the Government.

(2) Regulation based on maximum prices as referred to in Paragraph 1 above applies to calls to the end point of the public telephone network of the Party to the Proceedings, to which the terminal equipment of the called subscriber is connected, which calls are incoming calls from another public electronic communication network.

II.

(1) For newly concluded agreements, the Party to the Proceedings shall negotiate prices in compliance with the price regulation based on Part I of the Decision award and shall start doing so from the effective date of the Decision.

(2) In the remaining cases the Party to the Proceedings shall negotiate prices in compliance with the price regulation based on Part I of the Decision award and shall start doing so within two months of the effective date of the Decision.

Substantiation

In accordance with Section 51(1) and (2) of the Act, the Czech Telecommunication Office ("the Office") carried out an analysis of Market No. 9 - Call Termination in Individual Public Telephone Networks at a Fixed Location ("Market No. 9"), which it made public on the official board on 16 March 2006 under Ref. No. 1 514/2006-609/III vyř. and, upon notification to the European Commission, it issued it as Measure of General Nature No. A/9/04.2006-19 of 19 April 2006. The results of the analysis showed that Market No. 9 is not an effectively competitive market because there are undertakings with significant market power doing business on it. It follows from the nature of Market No. 9 that each service provider is an undertaking with significant market power because each of them has a 100% share of its network. The analysis also showed that prices disproportionately high and unfair to the end users are used on the market in cases where no price regulation is applied. For this reason, the administrative body proposed to apply price-control obligations, which it intends to impose in accordance with Section 51(3) of the Act.

By the administrative body's Decision No. SMP/9/04.2006-8 of 24 April 2006, which was issued under Ref. No. 11 475/2006-609/ V. vyř. and became final on 25 April 2006, the Party to the Proceedings was determined to be an undertaking with significant market power.

On Part I of the Decision award

On the basis of the result of the analysis, Measure of General Nature No. A/9/04.2006-19 was issued in accordance with Section 51(2) of the Act, proposing to impose the obligation to enable access to specific network elements and associated facilities under Section 84 of the Act, obligation to ensure transparency under Section 82 of the Act, obligation to ensure non-discrimination under Section 81 of the Act, obligation to maintain separate records of costs and revenues under Section 86 of the Act, obligation to provide supporting evidence for pricing calculations under Section 86(5) of the Act, and price regulation-related obligations under Sections 56 and 57 of the Act.

With respect to this proposal, the administrative body considered the proposed obligations. The obligation specified in Part I of the Decision award was imposed on the Party to the Proceedings through this Decision with reference to what is stated below. The imposition of obligations under Sections 51(3)(a) to (f) is the subject of separate administrative proceedings.

For determining the maximum prices, the administrative body used the input data structure based on Annex 1 to Measure of General Nature No. OOP/4/03.2006-3, in which the methodology of service costing and revenue settlement and of cost and revenue allocation is laid down and the structure of the information to be disclosed is determined. The prices were calculated on the basis of the LRIC model and fair profit was defined in accordance with Article 6 of the above-mentioned Measure. The LRIC method was chosen in order to identify an efficient operator's costs.

The applied method of price regulation using maximum prices for termination based on Section 58(1)(a) of the Act was chosen, because determination of a price using the LRIC model applied to

the termination services requires large amounts of data to fill the model. Their specific levels must be verified in detail by the administrative body in order to ensure that they are used correctly. In such a situation the determination of the maximum price appears to be the only possible solution.

To fill the LRIC model with data, when determining the maximum price on the market, the Office used as a basis the topology of the network of ČESKÝ TELECOM, a.s. as the largest provider (largest in terms of the public telephone network subscriber lines). The application of this method to other operators relied on the generally accepted principle by which the remaining operators' networks were built in a competitive environment and their efficiency is therefore at least as high as that of ČESKÝ TELECOM, a.s.

The determined prices reflect the effectively and efficiently spent funds, the specific risks and investment recovery within a reasonable period of time in compliance with Section 57(3) of the Act. The return on invested capital before tax (weighted average cost of capital WACC) was set at 11.18%, i.e. the amount set out in Measure of General Nature No. OOP/4/03.2006-3. The determination of the WACC is in keeping with the general practice in the electronic communications sector. Its value was determined as the arithmetic mean for the values used in the studies by Raiffeisenbank a.s. and CENTRAL EUROPEAN CAPITAL CZ, s.r.o. Both these studies were prepared for the Czech Telecommunication Office in 2005. The mean also comprised the WACC values determined for ČESKÝ TELECOM, a.s. by another four independent qualified entities, including Deutsche Bank, Patria Finance a.s., WOOD & Company Financial Services, a.s., and Morgan Stanley.

Part I of the awarded Decision defines the maximum termination prices. The prices are differentiated by the location of the access gateway switch and the end point of the interconnected publicly accessible telephone network and also by the high and off peak time. For the purposes of this Decision on price, there are definitions of the termination prices in the first paragraph of the Decision award. In the second paragraph of that part of the Decision the administrative body defined the calls regulated by the price-cap (the maximum prices determined in the first paragraph).

In the event that interconnection for termination takes place in a switch other than the local or last transit switch, the prices should be negotiated so that the resultant price is a sum of the agreed termination price (respecting the proposed Decision on Price) and the price for the corresponding transit.

On Part II of the Decision award

The Party to the Proceedings must negotiate prices in compliance with price regulation for the contracts to be newly concluded from the effective date of the Decision. In the remaining cases the Party to the Proceedings must negotiate the prices in compliance with price regulation within two months after the effective date of the Decision.

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With respect to the above, administrative procedure under Section 51(3)(g) of the Act was instituted against the Party to the Proceedings on 16 March 2006 in respect of the imposition of obligations related to price regulation on undertakings with significant market power. As set out in Section 51 of the Act, the undertaking whose rights and obligations are to be decided on should be the Party to the Proceedings. Notification of the commencement of the administrative proceedings was sent to the Party to the Proceedings and it contained an invitation for the Party to the Proceedings to express its view and propose evidence, for which it was granted a period of 7 days after the date of delivery of the notification.

On 23 March 2006, the Party to the Proceedings submitted its opinion on the institution of the proceedings.

The Party to the Proceedings stated that the results of the analysis published in a format other than a Measure of General Nature, as required by Section 51(1), second clause, of the Act cannot provide a basis for the imposition of an obligation on an undertaking having significant

market power in the relevant market. As the Party to the Proceedings also believes, the fact that the results were made public on the official board on 16 March 2006 cannot be considered as publishing under Section 51(2) of the Act, because consultation based on Section 131 of the Act was not completed. The Party to the Proceedings adds that publication in the Telecommunications Bulletin is the appropriate form of publishing the results of the analysis within the meaning of Section 125(2)(c) of the Act.

Referring to this objection raised by the Party to the Proceedings, the administrative body states that it commenced the administrative proceedings after performing an analysis of market No. 9 under Section 51(1) of the Act. Then, after completing the public consultation based on Section 130 of the Act, it published on the electronic official board the result of the analysis of market No. 9, reflecting the comments from the public consultation, including the opinion of the Office for the Protection of Economic Competition; it did so on 16 March 2006 on the basis of Section 51(2) of the Act under ref. No. 1 514/2006-609/III. vyř. With respect to the timing of the completion of the analyses of relevant markets as defined in the Act, the Office instituted these administrative proceedings on 16 March 2006. The administrative body granted the Party to the Proceedings a reasonable period for submitting its opinion. The process of analysis of market No. 9 was completed by publishing the result and the analysis was sent (notified) to the European Commission. Therefore the administrative body states that commencement of the administrative proceedings after publishing the result of the analysis – though before the effective date of Measure of General Nature No. A/9/04.2006-19 – does not involve any contravention of the Act; none of the rights of the Party to the Proceedings was infringed and it was given every opportunity to assert its rights under the legal regulations in force. Should any change be made in the results of the analysis on the basis of the notification, the Party to the Proceedings would have been granted an additional period of time to express its additional opinion. However, this did not happen. The text of the result of the analysis and the effective Measure of General Nature are identical.

The Party to the Proceedings requested an amendment to the second paragraph of Part I of the Decision as follows: “(2) Regulation based on maximum prices as referred to in Paragraph 1 above applies to calls to the end point of the public telephone network of the Party to the Proceedings, to which the terminal equipment of its called telephone subscriber is connected, which calls are coming from another public electronic communications network.”.

The administrative body granted this objection, but used the term “subscriber” instead of “telephone subscriber” and the term “incoming” instead of “coming”.

The Party to the Proceedings requested to add a paragraph 3 to Part I of the Decision as follows: “(3) In the event that interconnection for the purpose of termination takes place at a switch other than the local switch or the last transit switch, the prices shall be negotiated so that the resultant termination price is a sum of the negotiated termination price (respecting this Decision on Price) and the agreed price for the corresponding transit.”.

The proposed additional text relates to transit between switches and is not a part of the substantive definition of market No. 9. Inclusion of the proposed text in the Decision would amount to regulation, by the administrative body, also of certain services outside market No. 9. For this reason, the administrative body did not grant this objection and did not amend the Decision as requested by the Party to the Proceedings. However, this does not challenge the indicated price negotiation method itself.

The Party to the Proceedings requested to add a paragraph 4 to Part I of the Decision as follows: “(4) For the application of call termination prices, the principle of reciprocity shall apply to interconnection between fixed electronic communication networks.”

This request, proposed by the Party to the Proceedings, is superfluous. In the case of undertakings doing business on market No. 9, the administrative body used an approach which was identical to that taken toward the Party to the Proceedings.

The Party to the Proceedings drew attention to the incorrectly used term “for origination” in the eighth paragraph of Part II of the Notice of Commencement of Administrative Procedure. The correct term was “for termination”.

The administrative body substituted the correct term for the wrong one, as indicated by the Party to the Proceedings.

The Party to the Proceedings disagrees with the proposed level of maximum prices and substantially disagrees with the removal of the surcharge for CS/CPS services and the inclusion thereof in the LRIC model.

The purpose of the provision of the CS and CPS services is to provide conditions for competition to develop in the market for the public telephone services and thereby to enable alternative operators to provide comparable public telephone service to end users. Introduction and provision of the CS and CPS services is beneficial to all end users, including the end users served by the Party to the Proceedings as well as those served by alternative operators. For this reason, the administrative body spread the to-date costs in the form of surcharge for CS and CPS over all the calls originated and terminated in the network of the Party to the Proceedings.

The Party to the Proceedings disagrees with the calculation of the transmission routes on the basis of the road distances between the cities where the switches are located and requests that it (the Party to the Proceedings) should be responsible for calculating these input data.

The principle of the LRIC model is that the network must be efficient, including the length of the line between the switches. For example, in the 2003 inputs, there were several cases in which the distance shown in the calculation was more than twice the air distance.

The submission of the Party to the Proceedings included a figure depicting the actual circular topology based on the inputs adjusted by the administrative body. The inputs are shown as connecting lines between the local switch and the transit switch. However, the administrative body did not use the air distance, whose length would correspond to what is shown in the figure; instead, it used the road distance, which is always somewhat longer, as also indicated by the background data used for the calculation (bar charts comparing air and road distances, showing that the road distance is about 15% longer than the air distance).

The Party to the Proceedings also used the argument that the circular connection of local switches offers the advantage of a lower need for investing funds in trenches and cables and that the network is more reliable, including, in particular, better resistance to outages.

It must also be said that the model explicitly expects the local switches to be connected in a circle, with two transit switches connected to each circle. It is clear, therefore, that the model uses the same topology as used by the Party to the Proceedings. The Party to the Proceedings benefits in practice from the advantages offered by the circular layout, but these advantages are not comprised in the model. Duct sharing is only reflected in the model between the transport and access networks, whereas in practice ducts are also shared between individual levels of the transport network. A circular network at the same time enables optimum utilisation of the capacity of the circle infrastructure to which the individual switches are connected. The model calculates network capacity on the basis of traffic in the highest-traffic hour of the year, yet in the individual switches such a time occurs at different hours of the day and in different periods of the year, which is not reflected in the model. The LRIC model does not mirror reality. It goes far to simplify things and in the infrastructure area it tries to optimise the connection of a defined number of elements.

Then the Party to the Proceedings went on to explain in detail its views concerning the way to solve the issue of interconnection between transit switches.

The specific solution to the transport network of the Party to the Proceedings relies on a number of factors: some may be advantageous at present (new ducts do not need to be laid), while others may involve lack of efficiency resulting from historical development. The advantages resulting from specific layouts, e.g. duct sharing, are not reflected in the model. Duct sharing is only reflected in the model between the transport and access networks, whereas in practice ducts are also shared between individual levels of the transport network. The model must not copy inefficient features: its task is to optimise the costs of the infrastructure.

Responding to the reference made by the Party to the Proceedings to the documentation for the EER Model, “Study on the Preparation of an Adaptable Bottom-up Model for Interconnection and Access Pricing in European Union Countries – a final Report for Information Society Directorate

General of the European Commission by Europe Economics", dated April 2000 (the Party to the Proceedings used this reference at the "Investment Costs" input), the administrative body verified again the compliance of the model methodology and the data collection methodology. Consequently, the administrative body decided to add more precision to the calculation of the average distance of transmission routes between the transit switches by also including in the calculation the distances between the switches that are not directly interconnected within the network of the Party to the Proceedings, as the model takes such connections into account. After this adjustment, the value of this input increased by 7%. Nevertheless, the new value of this input had no impact on the resultant price.

The Party to the Proceedings disagreed with the value of the input of "Cost of Capital before Tax", calculated by the administrative body. It requests that this input data should be left as submitted by the Party to the Proceedings.

The administrative body did not grant this objection. The determined prices reflect the effective and efficient expenditures, the risks involved, and the recovery of the investments within a reasonable period of time in accordance with Section 57(3) of the Act. The cost of capital before tax is, therefore, one of the items reflected in the maximum price determination. The weighted average cost of capital (WACC) before tax used in the calculation was 11.18%, i.e. the level set out in Measure of General Nature No. OOP/4/03.2006.3. The determination of the WACC before tax complies with general practice in the electronic communications sector.

The Party to the Proceedings disagreed with the regulation of discounts at the inputs of "B19 – Fixed Costs of Processor – RCU – acquisition price"; "B23 Digital Termination Unit – RCU – acquisition price"; "B26 – Fixed Costs of Processor – LS – acquisition price"; "B29 – Costs of Connection Field (per 1 Erlang in the highest traffic hour) – LS – acquisition price"; "B30 Digital Termination Unit – LS – acquisition price"; "B33 – Fixed Costs of Processor – TS – acquisition price"; and "B37 Digital Termination Unit – TS – acquisition price", in Chapter 3: Economic Preconditions, and requests that this input data should be left as submitted by the Party to the Proceedings.

Substantial quantity discounts in cases of mass purchases is a pricing strategy commonly used by manufacturers and there is no reason not to include them among the inputs in the model. The Office had already made such an adjustment to the price of switches in its previous cost calculations. The fact that in the 1990s the prices were different from those in 2004 does not mean that the same discounts cannot be applied to other prices. The model is simplified and generalised, so that the inputs must be adjusted accordingly. Attention should at the same time be drawn to the fact that depreciation is determined in the LRIC model in each calculation for the first depreciation year, which may play an important role when the tilted annuity method is used; the remaining input conditions must therefore be set as if the network were just finished.

The Party to the Proceedings claims that the administrative body performed the specific calculations incorrectly.

The administrative body accepts the values indicated by the Party to the Proceedings.

The Party to the Proceedings agreed with the exclusion of the surcharge in the case in express delivery in inputs "B41:B43 – STM – acquisition price" in Chapter 3: Economic Preconditions.

The Party to the Proceedings drew attention to the fact that in the case of the inputs "B68 Network Management – Switches – acquisition price"; B69 Network Management – Transmission Equipment – acquisition price"; B70 Network Management – Infrastructure – acquisition price"; and "H19:H70 Operating Network Costs as Percent of Investment" in Chapter 3: Economic Preconditions, a change may occur in the value of the given investment and that, as a result, it would be necessary, whenever any adjustment is made to any of the inputs in the EER model, also to re-calculate the above inputs.

The administrative body accepted this comment.

The Party to the Proceedings submitted evidence to the administrative body, concerning the average life for input D19:D70 – Economic Life of the Asset in Chapter 3: Economic Preconditions, which was X years for 2004.

The administrative body used the 2003 value, which was X years, because no circumstances had meanwhile occurred, which would indicate any reduction of the useful life.

The Party to the Proceedings substantially disagreed with the adjustment of the value of costs in the case of inputs C19:70 – Costs of Installation in Chapter 3: Economic Preconditions. The Party to the Proceedings requests that the value should be left as calculated by it. In its submission (contained in Annex No. 1 to Evidence No. 1), the Party to the Proceedings included descriptions of network planning activities.

The administrative body made the adjustment on the basis of its findings obtained during state inspection of the inputs in the LRIC interconnection model. The costs of network planning and documentation are only represented by the personnel costs incurred in those activities and are not capitalised in the accounting records of the Party to the Proceedings, and as a result, they are included in the current year operating costs. Hence, in compliance with the accounting principles of the Party to the Proceedings, the administrative body included the network planning and documentation costs among operating costs. The administrative body would consider it methodologically incorrect, on the other hand, to include these costs in the installation costs in the LRIC model, because the model "capitalises" the installation costs, i.e. adds their value to the acquisition price of the asset and then, from that amount, it calculates the depreciation and cost of capital. The procedure used by the Office also complies with the documentation of the model, which the Party to the Proceedings refers to: the formulation on page 56 is "… (such as capitalised planning, …)". What is written on page 57 is not "capitalised planning" but merely "cost of planning and installing"; however, it follows from the nature of the matter itself that the network element acquisition costs must be specified by the same method. The administrative body, at the same time, took into account the data contained in Annex No. 1 to the submission of the Party to the Proceedings. It states that many of the activities comprised in the network planning costs are of operating nature – a fact that supports the administrative body's position that the costs of planning belong among current items rather than being part of the acquisition cost of the asset. The administrative body emphasises that the costs of planning were not excluded from the model: they were only shifted to operating costs.

The administrative body did not accept the comment by the Party to the Proceedings that the costs of network planning and documentation should be reflected in the model as the costs of installation; however, it did grant the second comment and, on the basis of the available data submitted by the Party to the Proceedings, it increased the costs of network planning and documentation.

On 30 March 2006, the Party to the Proceedings read the file and on 6 April 2006 it complemented its comments on the adjustments made to the input data by the administrative body.

The Party to the Proceedings reiterated its substantial disagreement with the calculation of the average lengths of the transmission routes between the LS-TS and TS-TS ("B97 – average length of LS-TS transmission routes in metres, irrespective of the nature of the territory" and input "B98 – average length of TS-TS transmission routes in metres, irrespective of the nature of the territory" in Chapter 2: Technical Preconditions; it did so on the basis of the road distance between the cities where the switches are located, and requested to use, in these inputs, the data calculated by the Party to the Proceedings, taking into account the actual topology of that Party's network. To support this request, the Party to the Proceedings points out the fact that the administrative body itself indicates in the substantiation of its Draft Decision on Price that "the model explicitly expects the local switches to be connected in a circle, with two transit switches connected to each circle", although in the calculation of the average length of the LS-TS transmission routes it utterly ignores this fact. The actual distances between the LS and TS switches are in fact longer, as the Party to the Proceedings believes, than the road distance (actually used in the calculation), because a circular path needs to be followed in the measurement. To demonstrate its assertion, the Party to the Proceedings uses the specific example of interconnection of two LSs at Písek to two transit switches in České Budějovice and Plzeň.

The LRIC model used for the calculations is based on the scorched node assumption. This principle maintains the topology and number of nodes in the network, but builds an efficient

transmission network anew in order to interconnect the nodes as needed for the existing traffic in the network, taking into account the achieved technological standard.

The model itself builds the efficient LS-TS transmission routes within a circular topology. In calculations on the "Transmission Electronics" and "Infrastructure" sheets, the model defines the number of the circles, the number of the nodes belonging to the individual circles, as well as the dimensioning of the transmission capacity of the individual circles. The required length of optical fibres in metres is calculated on the basis of the input of "B97 – average length of LS-TS transmission routes in metres, irrespective of the nature of the territory" (the D45 cell on the "Infrastructure" sheet). Calculation on the "Transmission Electronics" and "Infrastructure" sheets effectively increases the input "B97 – average length of LS-TS transmission routes in metres, irrespective of the nature of the territory" so as to obtain the transmission distance with each newly proposed circle. The resultant effective transmission distances then also include backup routes to both transit switches within the circles, which is achieved by multiplication by factor 4. This factor represents the transmission pairs in both transmission directions (see the formulas contained in cells C45 to E45 on the "Infrastructure" sheet). A more detailed explanation of the principles of modelling the transmission network is contained in Chapter 5 (pages 28-35) of the documentation for the EER model, "Study on the Preparation of an Adaptable Bottom-up Model for Interconnection and Access Pricing in European Union Countries – a final Report for Information Society Directorate General of the European Commission by Europe Economics", of April 2000, submitted by the Party to the Proceedings as Evidence No. 2 (hereinafter referred to as "EER model study"); the title of the chapter is "Modelling the Transmission Network".

It follows from the above that if the distances proposed by the Party to the Proceedings were used, the transmission distances would be disproportionately and unreasonably increased. These distances, as proposed, are already increased to reflect the circular topology, and the Party to the Proceedings wants them to be increased again through the LRIC model within the calculation of the effective transmission distances of the effective circles – which does not make sense. This would in fact duplicate the subsequent model calculation. Taking this into account, the example of the interconnection of the Písek LS to the two transit switches in České Budějovice and Plzeň (as brought forward by the Party to the Proceedings) is irrelevant.

The Party to the Proceedings disagreed with the use of road distances for the interconnections on the first network level, i.e. between the TS switches. It believes that its network solution provides savings, as distinct from the solution used by the administrative body. The Party to the Proceedings puts forward the argument that the interconnections between the TSs use the available physical routes and transmission systems, and that the transmission route is optimally configured on the cables of the first network level, using the line systems on that network level. Further, the Party to the Proceedings uses specific examples of actual interconnections to demonstrate its assertions. It states that there is no reason to use distance for an interconnection that does not physically exist in its network.

The administrative body refers again to the principle of the LRIC model, i.e. the scorched node assumption. According to that assumption, the network is built anew, efficiently and optimally, maintaining the topology and number of nodes in the network. As the efficiency of the solution calculated by the model is high, there is no reason to believe that the network solution proposed by the Party to the Proceedings would be more economical. Further, in view of the above, it is irrelevant to argue that there is no physical interconnection between the switches in reality, and it is likewise irrelevant to bring forward specific examples of actual interconnection to demonstrate the distances.

As to the efficient TS-TS transmission routes, the model itself builds them within a "ladder" topology (see documentation for the EER model, evidence No. 2 submitted by the Party to the Proceedings, page 29, fig. 5.1, and page 32, Chapter 5.2.3). Within the calculations on the "Transmission Electronics" and "Infrastructure" sheets, the model determines the interconnection of the individual nodes as well as the dimensioning of the transmission capacity. The required length of optic fibres in metres is calculated on the basis of the input of "B98 – average length of TS-TS transmission routes in metres, irrespective of the nature of the territory" (the E45 cell on the "Infrastructure" sheet). Calculation on the "Transmission Electronics" and "Infrastructure" sheets effectively increases the input "B98 – average length of TS-TS transmission routes in

metres, irrespective of the nature of the territory" so as to obtain the transmission distance. The resultant effective transmission distances then also include backup routes to both transit switches within the circles, which is achieved by multiplication by factor 4. This factor represents the transmission pairs in both transmission directions (see the formula contained in cells E45 on the "Infrastructure" sheet). A more detailed explanation of the principles of modelling the transmission network is contained in Chapter 5 (pages 28-35) of the "EER model study".

The conclusion is therefore the same as in the case of calculating the transmission distances of the LS-TS interconnections. It is obvious that if the distances proposed by the Party to the Proceedings were used, the transmission distances would be disproportionately and unreasonably increased. These distances, as proposed, are already increased to reflect the actual topology, and the Party to the Proceedings wants them to be increased again through the LRIC model within the calculation of the effective transmission distances of the effective "ladders" – which does not make sense. This would in fact duplicate the subsequent model calculation.

The Party to the Proceedings also expressed its view as to the administrative body's statement that duct sharing is only reflected in the model between the transport network and access network, whereas, in reality, ducts are also shared between the levels of the transport network. The Party to the Proceedings claims that, in the calculation of the B121 to D 121 inputs (total length of trenches [ducts, cable routes] for the transport network in the transmission sections RCU-LS, LS-TS and TS-TS – Technical Preconditions), this fact is taken into account on the basis of the total fibre optic cable lengths in the network of the Party to the Proceedings and on the basis of the number of fibre optic cables in the duct, i.e., the total duct length is smaller than the total length of the cables.

The administrative body notes the following.

The Party to the Proceedings disagreed with the administrative body's statement that no circumstances appeared to indicate any reduction of useful life in the case of inputs D19 to D70 Economic Life of the Asset – Infrastructure, in Chapter 3: Economic Preconditions. The Party to the Proceedings also disagrees with the related adjustment of the input. In the model inputs submitted in 2004 (Enclosure to Letter Ref. No. 298/2004-RIU-REG II vyř), the Party to the Proceedings indicated X years as the useful life of the infrastructure, i.e. the cables and the ducts, and explained that this figure is supported by the Company's depreciation schedule. Further, the Party to the Proceedings asserted that it would bring forward evidence to support this proposal and an explanation thereto, but failed to do so. The administrative body therefore used the same useful life as in the previous year.

The Party to the Proceedings did not agree with the administrative body's statement that the "LRIC model does not mirror reality" and "goes far to simplify things", … "so that the inputs must be adjusted accordingly". It brings forward a number of arguments to substantiate its disagreement. The first such argument is that the selection of the model was agreed with all the other licensed operators and the model was approved by the administrative authority. As the Party to the Proceeding asserts, it follows, *inter alia*, from the documentation for the EER model that the basic principles that are subsequently modelled in the calculation are identical with the basic principles used in its network, so that there is no reason to believe that the model is simplified and does not mirror reality. According to its own assertions, the Party to the Proceedings developed a data collection and input calculation methodology to fill the model with parameter values as accurately as possible and it does not make any "purpose-driven" simplifications in the calculations, so that there is no reason for the administrative body to embark on such simplifying practices. In addition, as the Party to the Proceedings argues, input parameter calculations that are as accurate as possible will contribute to identifying the most realistic interconnection costs. The Party to the Proceedings believes that in the reverse case a gap will develop between the resultant interconnection costs and the actual costs calculated by the LRIC methodology for the dominant operator.

As obvious from the very principle of the LRIC model's function, it is not a mirror reflection of an actually existing network. The model only maintains (according to the scorched node assumption) the topology and number of nodes in the network, but the interconnections between the nodes are built anew through the model calculations, and so is the dimensioning of the equipment for

the individual nodes: this is done effectively according to the requirements of the existing traffic in the network, taking into account the current technological standard. Hence, the task of the model is to design an effective network rather than to mirror the network of the Party to the Proceedings. The network that emerges from the modelling process may therefore not be a mirror reflection of the network of the Party to the Proceedings, although the Party to the Proceedings so asserts.

As to the simplification in the model, the administrative body insists on its assertion. The LRIC model is only an approximation of an actually functioning system, like any other already existing model. Approximation of a functioning network and its costs is involved in this case. This is also clearly indicated by the EER model study, where it is stated (among the model's main characteristics, for example on page 1 in Chapter 1) that the model should be flexible enough to be able to estimate the costs of different networks. Further, on page 7, it is stated that the model makes estimates of the incremental costs of the network architecture and the technology of an efficient operator. The "cost estimate" term is used consistently throughout the EER model study, so that no further examples are needed.

As to the adjustments to the inputs for the model, the EER model study contains examples that show the cases where only estimates can be used, due to the nature of the model. For example, it is written on pages 36 and 37 that problems may occur with fulfilling the routing factors for the networks to be used for leased lines, which in them are point-to-point connections from one place to another and use the network in a manner that is absolutely different from PSTN traffic. These routing factors can therefore be only determined by estimates.

Nevertheless, the administrative body welcomes the effort of the Party to the Proceedings to fill the model as accurately as possible.

Further, the Party to the Proceedings disagreed with the administrative body's assertion that at the different switches the traffic of the highest-traffic hour of the year "sets in at different hours of the day and in different periods of the year, which is not reflected in the model". The Party to the Proceedings argues that the network must be dimensioned to traffic load in the highest traffic hour and that there is no need to distinguish load levels with respect to hours or days. According to the Party to the Proceedings, such an approach does not involve simplification and is in fact absurd, as most of the switches have their highest-traffic hour in the early evening and, in addition, the distribution of the load during the day follows about the same pattern during the year, so that there is no reason to distinguish between hours or days.

The administrative body did not challenge the calculation of the input of traffic in the highest-traffic hour of the year, as the Party to the Proceedings believes: it only stated that there are reserves within the network that can be utilised but are not reflected in the model.

The Party to the Proceedings also expressed its views as to the adjustments of discounts on the acquisition price of the switches. In its view the model builds an entire network for the calculation period and it is therefore necessary also to take into account the conditions prevailing in the given period: the considerations cannot be based on the discounts that were guaranteed in the past. In addition, the Party to the Proceedings believes that the administrative body performed the adjustment incorrectly and the resultant values differ from the calculations made by the Party to the Proceedings and submitted on 20 March 2006 as Addendum No. 28.

The administrative body insists on its previous statement. The differences in the results of the calculations made by the Party to the Proceedings and the administrative body are due to different rounding.

The proposals and objections made by the Party to the Proceedings and its statements in respect of the evidence supporting the decisions made during the administrative proceedings were addressed by the administrative body as indicated above and the administrative body prepared a draft decision in this matter.

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Under Section 130 of the Act and in accordance with the Czech Telecommunication Office's rules for maintaining consultations, the administrative body published on 27 March 2006 the draft decision at the discussion site, including invitation to submit comments at the site.

Most of the comments were related to methodological issues, related to the method of determination of the maximum termination prices and prices for call transmissions between two transit switches in the case of the call termination service. The administrative body adjusted the proposed decision to reflect the outcomes of the public consultation.

All the comments and the manner they were addressed were made public in the comment settlement table at the discussion site on 20 April 2006.

The Party to the Proceedings was given an opportunity to express its view in accordance with Section 122(5) of the Act. The Party to the Proceedings familiarised with the file on 20 April 2006. On 26 April 2006 the administrative body received the opinion of the Party to the Proceedings, where the said Party referred to its previous statements. It highlighted certain parts of the text in the Substantiation as trade secret and requested that they should be treated accordingly.

The administrative body decided as indicated in the Decision award. It did so, with respect to the above, in compliance with the key principles based on the legal framework of the European Communities, seeking to substitute for the absent action of economic competition, to create conditions for appropriate functioning of economic competition and to protect users and other market players until a fully competitive environment is created.

Advice on Remedies:

No remedy is allowed against this Decision.

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Czech Telecommunication Office
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[*signature*] *Pavel Dvořák*
PhDr. Pavel Dvořák, CSc.
Chairman of the Council of the Czech Telecommunication Office