Strategic Review of Telecommunications Phase 2

Response to Annex B, "List of questions"

1. Do you agree with Ofcom's proposed principles for regulation of telecoms markets?

1 a) What regulatory role should Ofcom play in the wider telecoms value chain?

Ofcom's role is necessarily limited to dealing with the effects of the network on the value chain. This is, however, a wide range of influence. The methods of connection into the network for the suppliers upstream in the value chain, the transport of that data through the core network, interconnections to access networks, and the ability to use and connect to those access networks for the consumers all fall under this remit.

Obviously any bottlenecks in the 'traditional' telecom area will have an effect not only on that area, but also in all other businesses in the value chain – i.e. an unregulated dominance in one area can effect all other areas in this value chain. Ofcom must remove these bottlenecks where possible, opening them up to competition, and where this is not possible, must regulate to ensure the dominance of one player in the telecoms arena does not allow them undue influence over the rest of the value chain.

1 b) How should Ofcom reflect differences in competitive characteristics in different geographic areas?

The challenges of ensuring a well functioning telecoms market vary across the UK. In particular, areas with a geographically dispersed consumer population are unlikely to be able to support competing access or 'middle mile' infrastructure, due to the high costs of providing an alternative to the incumbent. Because of this, Ofcom needs to put in place a regulatory framework in this area to enable services competition over the incumbent's access and 'middle mile' network. (Where middle mile is defined as the area of network between the access infrastructure and the core network.)

In areas where the consumer population is more densely gathered, 'middle mile' infrastructure is competitively available, and it is economically viable for alternative access infrastructure to be put in place. However, this may or may not presently be in place. A regulatory regime in this area must not provide a disincentive to investment in access infrastructure.

To these ends, an appropriate solution would seem to be:

- **Wholesale access to access infrastructure to be carried out across the country, with nationally averaged prices**
- **Wholesale access to 'middle mile' infrastructure to be available at regulated prices in areas of dispersed population**

This solution ensures that the access infrastructure can be used for services competition across the country, while acknowledging that 'middle mile' access is only required in certain areas. It will also not disincentivise investment in alternative access infrastructures where viable, as the nationally averaged wholesale price is likely to be capable of being undercut by a new entrant.

1c) What factors need to be taken into account when considering the scope of demand and supply-side substitution in telecoms markets on a geographical basis?
The factors should include somewhere a service view, based upon a "basket" of applications and uses such that the channel delivery technology becomes of secondary importance. This would give greater depth to the understanding of the information otherwise gained on supply side substitution on a geographical basis. Measure the use, behaviour and traffic of the goods rather than the transport. The basket" should be updated as the technology revolution progresses.

1d) To what extent would it be appropriate in the future to take into account differences in competitive conditions in different areas through (i) the aggregation of similar geographic areas or (ii) through different remedies?
Citizens and businesses should have equality of access and accordingly both options (i) and (ii) could come into play. A limited number of remedies could be all that is required for a limited set of aggregated geographical areas which between them account for the full range of similar problems.

1e) Would you support a requirement to provide Ofcom with data on particular products on a geographic basis as part of the regular reporting requirements?
Yes. Also please consider services as well as products (see answer to 1 e) above. Convergence will redefine many of the items to be measured.

What is the correct level of disaggregation?
The levels at which one can discern a differentiation of technology or of services which the customer in the market sees as alternative market offerings.

2. Where and to what extent should Ofcom rely on ex post competition law rather than ex ante regulatory conditions?
Ex post competition should be relied on to provide remedies on matters of principle where competitors are so disadvantaged that market dominance is maintained or achieved. Market disruption must not deter deploying the remedies. The market is imaginatively resilient so regulators don't have to construct the outcomes, just the boundaries.

3. In what circumstances would it be appropriate for Ofcom to make a reference under Section 131 of the Enterprise Act?

Ofcom has rightly recognised that any new regulatory regime will operate most effectively with the co-operation of the incumbent.

If this is forthcoming, it should not be necessary for Ofcom to use the Enterprise Act. However, if the incumbent is unwilling to give this co-operation (and cannot give valid reasons overlooked by other respondents to this consultation) then it would be appropriate for Ofcom to make a reference under Section 131 of the Enterprise Act, to ensure the UK has a well functioning telecoms market.

4. Should Ofcom adopt a broad approach of focusing regulation on enduring economic bottlenecks while tackling the problem of inequality of access head-on?

Yes, provided Ofcom continually assess these bottlenecks as to their existence and effect, and also as to whether a different regulatory approach can help to develop alternative routes that bypass these bottlenecks.

5. How can real equality of access be achieved at the product level?

5 a) Do you agree with Ofcom's definitions of the various forms of equivalence?

Yes.

5 b) Do you agree that equivalence of inputs can deliver more effective equality than application of equivalence of outcomes?

Yes. As explored in the consultation document, equivalence of inputs ensures BT is incentivised to produce high quality products for all of its retail customers, including its own retail arm.

5 c) Do you agree with the principles proposed on where equivalence should be applied and the specific suggestions for individual products?

The RDAs agree with the principles proposed. We do not feel able to comment on all of the suggestions for individual products, but the suggestions for LLU, DataStream and wholesale leased lines seem appropriate.

5 d) How do you suggest the principle of equality is achieved for 'associated products' that BT does not depend on (such as migration products)?

Associated products will necessarily require greater regulatory involvement, to ensure that the incumbent does not disadvantage competitors.

The alternative approaches detailed in Annex G are appropriate, though a varying combination of each would appear to be needed on a case by

case basis for the associated products. However, it should be stressed that where possible, products should be defined such that equivalence of input can be used, i.e. BT Retail would purchase the same product as any other operator.

6. What behavioural changes by BT do you believe would be necessary to achieve real equality of access?

Changes must include a commitment to transparency and effective methods of partitioning the wholesale and retail arms of the company. Ofcom should take responsibility for reviewing to what extent inequality of access is a consequence of BT's structure, and therefore the extent to which that structure needs to be modified.

7. How should Ofcom reflect the competing considerations of efficient investment and consumer protection in determining the regulated returns that BT may earn from its network?

The RDAs are concerned with increasing the size of the UK economy, by improving the productivity and competitiveness of UK business. The means to achieve this aim in this case are, however, aligned with the needs of the consumer, as championed by Ofcom. UK business needs rapid access to next generation networks to enable them to benefit from the increased productivity this can bring. Equally, the access to these networks must not be priced at a level where UK business cannot be competitive. As can be seen, this means that we too must accept a trade off in determining the regulated returns of BT from its network.

To this end, it seems appropriate that regulation of the current access network, which will receive only incremental investment, should be weighted heavily to providing the consumer with inexpensive services. The next generation access network regulation needs to reflect, however, the various risks that the incumbent faces in putting it into place. Equally, regulation should not stifle other players entering this area.

The approach outlined in our response to 1b would seem to apply here – it encourages both the incumbent and other players to invest in next generation access where alternative access networks are viable. This area would obviously need to be examined again as these networks are put into place, to ensure that rural areas also receive the benefits of a new access infrastructure.

Regulation of the core network requires an approach finely balanced between the two competing needs of UK business. The RDAs believe a period of consultation between Ofcom and the industry should be used to devise a fair rate of return for BT.

Taking a pro-competitive approach to access and interconnection to BT's 21st Century Network would seem the best way to ensure that regulation of this area can be light touch.

8. Do you agree with Ofcom's proposed approach to current generation broadband?

8 a) What should Ofcom's approach be to naked DSL?
Naked DSL is likely to become an important product in the future. A wholesale product built around this would seem to be needed, though it is unlikely in the short term that there will need to be significant changes to cover the common cost of the PSTN network – the number of consumers not requiring a traditional voice service is likely to be low for some time. Ofcom is right, however, is saying this issue will need to be examined when VoIP products become a mass market solution to voice calls.

8 b) Should there be different regulated wholesale products for current generation broadband in different locations?
No. See response to 1b.

8 c) How should the potential lack of equivalence faced by LLU operators in a 21st Century network environment be addressed?
RDAs have a preference for option 2 (see fig 17) as this enables maximum service innovation and rapid migration of customers. However, we accept that the costs for this approach are not at present known. If the costs under this model are prohibitive, we would be reluctant to move to option 3, due to the stifling of innovation.

9. Do you agree with Ofcom's proposed approach to deregulation of voice services?

9 a) Do you agree that Ofcom should review regulation of retail voice markets in 2005?
Yes.

9 b) Do you agree with Ofcom's proposals for deregulating call conveyance markets and wholesale IDD?
Yes.

9 c) When would it be appropriate to remove the requirement on BT to provide indirect access?
RDAs do not feel able to comment on this issue.

9 d) How should PSTN-specific regulation evolve under NGNs? What should next generation CPS and WLR products look like?
RDAs do not feel able to comment on this issue.

9 e) What are the prospects for increased competition for voice services

provided using broadband access products (such as LLU and the evolution of DataStream)? What conditions and transitional arrangements would need to be in place to allow service providers to secure access on the basis of commercial terms rather than PSTN-specific regulated products?
RDAs do not feel able to comment on this issue.

9 f) How should Ofcom ensure competition in areas where alternative platforms were not in place?
As digital convergence progresses, the service rather than the technology or delivery channel will become the dominant feature of the customers' consideration for procurement.

9 g) When do you expect fixed-mobile substitution to result in a single economic market for voice call origination?
RDAs do not feel able to comment on this issue.

10. Do you agree with Ofcom's proposals for deregulation of business voice services?

10 a) Has the voice market for large business become more competitive since Ofcom issued its large business pricing statement, necessitating the conduct of a new market review?
RDAs do not feel able to comment on this issue.

10 b) What wholesale inputs should be provided on an equivalent basis before BT should be granted greater freedom in relation to the pricing of voice services to large businesses?
RDAs do not feel able to comment on this issue.

11. How should regulation of narrowband internet evolve as networks migrate to NGNs, and how will functional, low bandwidth internet access be provided in future?
Regulation of narrowband internet access should remain in place for present access networks. At present, the most commonly used broadband access product is still not available for all areas (though the areas it is not available are very few), and to remove regulation on the only real alternative for high users in this area would be inappropriate. The exact method of delivery of low bandwidth access in the future is unclear. If there is significant investment in a next generation access network, it may be that the cost of providing a 512kB service compared to a 56kB is negligible, which would remove the need for low bandwidth products. However, this area is still uncertain, and RDAs await further developments.

12. How can the arrangements for access and interconnection to next generation networks best address our proposed regulatory principles?
The surest way to best address the proposed regulatory principles is to have sound appropriate information. The arrangements must include a useful set of reporting measures for the competitors to answer to.

It is not clear at this point where bottlenecks in the NGNs may occur. It is necessary to ensure that Ofcom has in place a structure that, during the early stages of development of NGNs, enables all players to compete equally. However, in those areas where competition is, following the roll out of the NGN, shown to be robust, regulation should be rolled back as soon as possible.

13. What should Ofcom's regulatory approach be to next generation access networks?
It should allow for unfettered future development as well as freely balanced price competition.

13 a) In what circumstances should Ofcom forbear from regulating next generation access?

13 b) How important is it that the investment be made contestable; is this achievable?

13 c) How should Ofcom regulate next generation access if market power were to emerge in this market?

13 d) How might structural options help to eliminate the problems of monopoly access assets being owned by vertically integrated operators?

14. What set of wholesale access services should BT be required to provide in order to promote competition in the business market?

15. What can be done to facilitate the migration of complex corporate services (e.g. VPNs) between suppliers?
Reduce costs of transfer, including implicit costs, e.g. being tied to a term contract.

16. Are any alternative structures for call termination appropriate? Could evolution to IP interconnection introduce market mechanisms that make intrusive regulation unnecessary?
RDAs do not feel able to comment on this issue.

17. What approaches should Ofcom adopt to reducing search and switching costs in telecoms?
Approaches like those used to tackle similar problems in the privatised utilities (gas, electricity) and banking services.

18. What should be the arrangements for funding the USO in future?

A uniform service rate charged on the user community would enable a fund to be built up which will pay for USO. This ensures transparency of purpose and accounting.

19. How could competition for the delivery of the USO be organised in future?

If there is an external fund (as above) to pay for USO, it would be appropriate for the largest service providers and the regulator to form a framework agreement as to the funding available. However, any requirement to provide service will place a burden on the company that takes it on. To this end, there are a variety of methods to achieve some fairness, and minimum effect on the market.

Requiring the single largest supplier to provide a service would not always be appropriate – the burden of the USO would be inappropriately placed solely on one company when, as a purely indicative example, Company A has 52% market share, and Company B 48%.

It would seem that once a company has come within a certain percentage of market share of the largest supplier (exact amount to be decided in consultation with the industry) the USO should then be imposed upon them also.

However, this situation brings new difficulties – which of the companies should have to provide a service to any individual client? The possibility of a round-robin arrangement, or an approach targeted at who has the infrastructure needed closest to the client, may be appropriate in this case.

20. Should mobile technologies be used to help address the existing USO?

Yes. Supply substitution is a valid option.