



**Ofcom's Consultations
on
Wholesale Mobile Voice
Call Termination**

BT's response

17 August 2005

BT would welcome comments on this response. Comments should be addressed by e-mail to Alan Lazarus at alan.lazarus@bt.com

Wholesale Mobile Voice Call Termination:

- Ofcom's proposal to modify the charge control conditions
- Ofcom's preliminary consultation on future regulation

This document comprises BT's response to Ofcom's two consultations on wholesale mobile voice call termination, issued on 7 June 2005¹.

Section 1 below addresses the principles of price control on mobile call termination and argues in favour of a long-term control.

Section 2 sets out BT's answers to Ofcom's four questions in the *charge control* consultation.

Section 3 provides answers to Ofcom's questions about the *future regulation* of mobile call termination.

Executive Summary

BT believes that Ofcom should impose a four-year charge control on voice call termination services from 1 April 2006, and that this should be applied irrespective of the technology used to provide the service.

If, however, Ofcom decides to implement only a one-year control, this should *not* simply be a freeze of charges at existing levels. We believe the control should, instead, provide customers with lower charges, because current rates are still well in excess of costs.

A continuation of recent trends, and the costs of 2G voice call termination, suggest reductions of around 10% are warranted.

This would provide customers with savings of around £100m in 2006/7.

¹ "Wholesale mobile voice call termination - a proposal to modify the charge control conditions", hereinafter referred to as 'the *charge control* consultation'; and "Wholesale mobile voice call termination - preliminary consultation on future regulation", hereinafter referred to as 'the *future regulation* consultation'.

1. Price Controls on Mobile Termination

Ofcom proposes that the voice call termination charges levied by the mobile network operators are frozen for 12 months, so that the rates which will apply at the end of the current price cap (which ends on 31 March 2006) are carried forward for another year. Ofcom has arrived at this proposal on the basis that it believes there are, "reasonable arguments in favour of both lowering the current controls and of raising them"². We do not believe the arguments are so finely balanced that a further year is needed to weigh up their relative merits. Even if a one-year extension of the existing control were justified (which we believe not to be the case), BT believes it should take the form of a "rollover" of existing controls and therefore apply the same criteria as were applied at the start of the control.

There seem to be two central issues raised in the consultations:

- whether to set a new price cap at all; and if so
- what value of 'X' should apply if any further price cap is set.

Ofcom's proposal amounts to the setting of a further price cap of one year's duration, and effectively setting an 'X' of RPI.

BT agrees that there is a need for a price cap on call termination charges for the reasons set out by Ofcom and on which we have commented further in response to the questions below. We believe there is a wide consensus for this regulation to be continued. However, we believe that the setting of a one-year price cap should only be used in extraordinary circumstances given that it merely postpones issues which will, in any case, need to be decided within a short time. BT would suggest this is not such a time.

One-year price caps are generally undesirable as they do not represent any form of 'incentive regulation'. This is because they are too short a period to provide a stable framework against which operators may seek to outperform the efficiency targets implicit in any cap. It also seems to us to be administratively expensive, as no sooner has one consultation been completed than another one on the same issues will need to be initiated. The UK pioneered price caps, and they have been adopted around the world; we do not think they should be forsaken in favour of other forms of price control, except when there are particular and exceptional circumstances (neither of which seems to pertain here, as we explain below).

We also note that the effective value of 'X' at RPI has been determined, not by use of any modelling analysis, but because it strikes, "the best balance between the arguments"³. In effect, Ofcom seems to be saying that, 'the balance now should be an 'X' of RPI, and over the coming 12 months we will come to a more considered view as to what X should be for the medium term'. We do not consider either that this is the right balance now, or that Ofcom needs more time to justify a price cap for the period from 2006 to 2010.

² The *charge control* consultation, paragraph 4.27

³ The *charge control* consultation, paragraph 4.27.

1.1 Justifying a delay

The most likely justification for a one-year postponement of a decision is that the year in question will provide Ofcom with valuable information needed for the regulatory task at hand. This should be information that could not otherwise have been available to Ofcom – that is, it comes from 'waiting' and learning from what is revealed by the actions of suppliers and by the market. The passage of time always brings more forward information, but this does not mean decisions should always be postponed. For incentive regulation to be set aside for a time, the period in question ought to be a critical time and one that will not be repeated in the near future.

In our view, Ofcom has not set out why 'waiting' a year is so important. In particular, for the reasons we give below, we do not believe the 3G modelling exercise is necessary to determine voice charges in 2006/7 and beyond.

Delay is certainly not without cost for consumers. Our approximate calculations are that price reductions justifiable on the information already known to Ofcom, would save fixed customers alone some £100m⁴ in 2006/7. It is therefore worth reviewing briefly the arguments that Ofcom says it is balancing when it proposes to postpone its decision:

1.2 Central arguments

The arguments in favour of reducing call termination rates are provided by an updating of the 2G LRIC model by Ofcom. This appears to show that the pence per minute cost of call termination is **4.58** for 900/1800 MHz combined networks (Vodafone and O₂) and **4.92** for 1800 MHz networks (Orange and T-Mobile).

Comparison between Ofcom's estimated costs and proposed call termination charges

	Vodafone & O ₂	Orange & T-Mobile
proposed charges	5.63ppm	6.31ppm
estimated costs*	4.58ppm	4.92ppm
differential	22.9%	28.3%

* excludes "network externality mark up"

All data derived from Ofcom's charge control consultation⁵

The proposed charges are thus 23% to 28% greater than cost. Around 12 percentage points of the excess over costs derives from a "network externality allowance" which represents a mark-up on costs, allowed by Ofcom to encourage mobile operators to expand their customer numbers. Given that penetration of mobiles is now so high as to be sometimes reported as "greater than 100%", we do not believe that a surcharge on fixed line customers (whether they are customers of BT or of other operators or service providers), can be justified any longer.

So, Ofcom's 2G cost modelling unambiguously points to a price cap that offers customers material price reductions.

Ofcom, however, considers that the introduction of 3G networks "is likely to result in an increase in the unit costs and hence efficient charge level of voice call

⁴ The value of a 0.6ppm reduction on volumes of 4,000 millions of minutes per quarter.

⁵ Figures 4.1 & 4.2 on pages 30-31 of the *charge control* consultation.

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termination"⁶. This is described as a migration effect – in other words, these are costs incurred by mobile operators as a result of introducing 3G networks. Ofcom therefore considers that customers making voice calls to mobile networks should forgo price cuts which they would otherwise have enjoyed because the MNOs are bringing in their new 3G networks.

We do not consider that this is a reasonable argument for the reasons we have set out in our response to Questions 8 and 9 in the *future regulation* consultation (below). We believe that new technology should not increase the price of voice calls and Ofcom should set call termination charges on the basis of 2G costs alone for the period up to 2010. In this respect, a comparison with the treatment of fixed networks is illuminating:

1.2.1 Comparison with the regulation of fixed networks

BT is about to replace its legacy networks with a single IP-based network in which multiple services will be carried over the same platform. There is a close analogy between this development and the move of mobile networks from 2G to 3G, in that end-customers will not, in general, be able to tell which network they are using. But in the case of the fixed network, it has not been suggested that BT's costs would rise in the long term as a result of introducing the new technology⁷.

In BT's case, Ofcom consulted explicitly on rolling over the existing network caps and on how to treat the impending technology change⁸. Ofcom took the decision not to continue the existing controls for a year in the hope that better information on the costs of the new network would become available. It also decided to model narrowband termination on the assumption that existing PSTN technologies continue, regardless of the underlying technology. This approach became known as the "technology neutral model". For BT, Ofcom is now proposing a 4-year price cap to last to 2009. The costs used are on the basis of modelled PSTN costs, despite the fact that BT is likely to have replaced its network and moved to all-IP platforms by the end of the control. The issue of whether and how to regulate new services that are based on the new network platforms, is being left until a later date.

We understand and have supported this approach. The time to consider the costs of the new network will be when the older ones are close to being retired, not when the new networks are being introduced.

1.3 'X' for a one-year price cap

If there is a genuine need for a very short term price cap whilst Ofcom considers its policy for the medium term, we feel that the current price cap ought to be extended at the same rate of decline in charges as settled by the Competition Commission in

⁶ The *charge control* consultation, paragraph 4.17.

⁷ Indeed, in relation to mobile networks, many analyst reports comment that 3G will improve the network economics relative to 2G.

⁸ "Review of BT's network charge controls: Explanatory statement and Notification of proposals on BT's SMP status and charge controls in narrowband wholesale markets" (issued 23 March 2005)

2003. That is, any control ought to have applied an "X" consistent with that which has been in place in recent years. Consequently, we believe that reductions in termination charges of circa 10% are entirely warranted. We calculate that this would result in a saving for fixed customers alone, of around £100m in 2006/7.

2. Questions posed in the *charge control* consultation

Question 1: Do you agree that there continue to be separate markets for wholesale voice call termination on each MNO's network (or, where the MNO operates both 2G and 3G networks, across both networks) and that the geographic extent of each market matches the scope of each mobile termination provider's network(s)?

We agree that, with current technology, there will continue to be separate markets for wholesale voice call termination on each MNO network⁹. We do not consider there to be separate markets for 2G and 3G voice call termination, as the calling party/network has no knowledge or control over the technology used for termination and, in any case, the EU framework provides for regulation to be technologically neutral.

Technological constraints currently limit the ability of those who pay for mobile voice calls to switch between operators. These constraints also mean that, under the calling party pays (CPP) arrangement, voice calls to a specific mobile number can only be terminated on the 2G and 3G mobile networks of the operator to which that number is registered/directed. Therefore a separate market exists for voice calls to each mobile operator's network.

Question 2: Do you agree that each of the 2G MNOs continues to have SMP?

We agree that each MNO continues to have SMP. The source of this market power is the CPP arrangement.

CPP creates a disconnect between the person bearing the entire end-to-end price of the call - the calling party - and the person receiving the call. It is the person receiving the call who chooses the network to subscribe to and therefore the network that terminates the inbound calls (which determines the price of the call). This means that there is little scope for downward pressure to be exerted on the price charged by the MNO for the termination element of the end-to-end price of calls, simply because the called party does not bear that element of the cost of service. Ofcom cites evidence (paragraph 3.33 of the *charge control* consultation) that only 2% of such subscribers spontaneously mentioned the cost of inbound calls as influencing their choice of network operator.

Question 3: Do you agree that Ofcom should extend the existing charge control on 2G voice call termination by one year?

BT does not support a one-year extension of the existing charge control.

⁹ We cannot, however, exclude the possibility that in the future, some form "technological portability" may exist and be sufficiently cost-effective to enable a customer to call a mobile number without terminating the call on the mobile network of the receiving customer; at which time a review of market definition may be warranted.

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The current rollout and adoption of 3G technology is not a sufficient reason to postpone the imposition of an appropriate new charge control. In addressing the BT fixed network, Ofcom has decided to use PSTN costs as the basis for calculating the next Network Charge Control, despite the fact that the technology of fixed calls is expected to change from PSTN to NGN over the next 4-5 years (see paragraph 1.2.1 above). For consistency with its policy towards fixed networks, Ofcom should abandon its 'wait and see' position in delaying the imposition of a new 2G mobile charge control simply because of increasing use of 3G networks¹⁰.

Ofcom's desire to postpone a decision, based on uncertainty as to how 3G costs will impact with 2G costs, is also inconsistent with its approach to setting costs which BT is allowed to recover when it retails inbound services for terminating operators (the "NTS Retail Uplift"). Here, the same types of issues arise and there is uncertainty over costs due to the substitution of narrowband services by broadband internet access. Nevertheless, Ofcom has proceeded with a new set of charge controls which will apply for a number of years.

As these examples show, Ofcom has set price caps for fixed services in similar circumstances to those which apply to mobile termination services. It should not set a one-year price cap for mobile services.

In fact, Ofcom's Option 2 ('impose a 4-year charge control'), provided it takes account of the need for material price reductions, is the only legitimate option, given that 2G is more than likely to dominate costs in such a period. It also has the advantages of both providing an appropriate length of time for Ofcom to assess the impact of 3G costs needed for any subsequent control, and ensuring that consumers do not forego price reductions because of issues or questions around 3G.

Question 4: Do you agree that the Target Average Charges should remain unchanged?

No. Mobile termination charges are still too high, reducing consumer welfare (especially for those fixed line users without a mobile) and encouraging excessive substitution of fixed calls by mobile calls, while at the same time the asymmetry effectively results in mobile subscriber-acquisition costs being subsidised by fixed line customers. One industry should not subsidise the other but this is the effect of cost-based termination of fixed networks on the one hand, and charges in excess of costs for mobile networks on the other. We believe price cuts of around 10% are warranted in 2006/7.

One reason that mobile termination charges are still so high is the externality surcharge, the original rationale for which was to help promote subscription to mobile phones by subsidising MNOs' subscriber acquisition costs. However, the regulatory engineering of still higher mobile adoption is not a realistic or sensible target for which to aim. With around 80% of adults in the UK now owning one or more mobiles, virtually all adults who want a mobile already have one and the rationale for the externality surcharge is no longer valid.

¹⁰ Such use of 3G networks is, in any case, currently still very low, with T-Mobile not yet having launched a consumer 3G offering.

3. Questions posed in the *future regulation* consultation

3.1 Addressing SMP (Ofcom Section 3)

Question 1: Could RPP principles be made to work to the advantage of consumers in the UK? If so, how?

Question 2: Is it realistic to believe that a competitive market for wholesale termination of voice calls could be made to operate successfully. How might such arrangements work?

Question 3: Is VoIP likely to have a significant impact on the market for mobile voice call termination during the period to 2010? What are the possible obstacles to this outcome and how might industry or Ofcom overcome these?

Question 4: Are there other options, not considered elsewhere in this consultation document, for removing the underlying causes of SMP?

BT appreciates that Ofcom does not wish to impose regulation if it can be avoided. Indeed, at the time of a preliminary consultation, it is quite right to consider all possibilities other than direct price controls. However, we do not know of any realistic options at the present time, for removing the underlying cause of SMP which is that the purchaser of call termination services cannot choose his or her preferred supplier.

As Ofcom recognises, one route to removing SMP would be to bestow choice on that purchaser of call termination, thus making call termination services subject to competitive pressures. If some form of call termination bypass were available, the caller (or originating operator) would select an alternative operator to deliver the voice call, avoiding use of the called party's operator. It would require access to the HLR of the called party's network operator, and changes to the 'attach procedure' which governs the process by which mobile users' handsets (virtually) attach themselves to a network. However, a mobile phone can only attach itself to a single network at a time. This therefore means that, using the cost-effective technology currently available, it is impossible for the called party to receive information (such as call waiting notification) whilst making a call using their network operator¹¹.

RPP is the most obvious possibility to rectify the causes of SMP, but it is not clear to us that there would be benefits in mandating such a regime in the UK rather than imposing regulation on call termination rates. That is, the overall cost of forcing competition into the supply of these services by mandating RPP might be higher than those associated with price cap regulation. This also applies to ideas such as the imposition of multiple SIM cards and/or the introduction (and, presumably, regulatory management) of common, shared or duplicated location registers.

¹¹ It is also unclear whether reversion of the phone's attachment to its original network would be automatic. If a manual intervention is required once the call is completed (by either the caller or subscriber) the method is, we believe, unlikely to be widely used.

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On the assumption that there are currently no other options which remove SMP, we suggest that Ofcom may wish to discuss the introduction of RPP with the mobile operators to be clear whether or not this might be an alternative. In our view, however, the most likely means by which any solutions may emerge are if the MNOs are given an *incentive* to devise mechanisms which either allow calling parties, or fixed operators operating on their behalf, to choose between suppliers of call termination services.

This suggests that Ofcom needs to indicate that it will impose a price cap for these services, including specifying the levels involved, but that it makes clear it is prepared to waive these controls if suppliers do propose alternative arrangements which provide choice for purchasers. Without knowing the regulatory obligations which will apply in the absence of such innovation, we feel that it is unlikely that new solutions will be forthcoming from the industry. It may therefore be important that, at an early stage in this process, Ofcom sets out the regulation which will otherwise apply.

We do not understand exactly how VoIP might have a bearing on this regulatory issue. The key issue is whether it would give calling parties choice when they need to purchase call termination. VoIP may mean that on some occasions customers will not need to purchase call termination services from an MNO, effectively because the called party may be paying (in which case VoIP is, essentially, a form of RPP). However, this does not mean there will be no need for regulation where the called party is not paying for inbound IP service or if the calling party cannot make an "IP call"¹².

This position would, however, not pertain if calling parties could affect this situation by having the decision-making powers as to whether to by-pass pence per minute rates, which could, in turn, put pressure on call termination prices. However, it is not clear how this situation might come about and we suggest that Ofcom considers the incentives for the adoption of VoIP. Our initial view is that there seems to be relatively little incentive for the called party to push for a more cost effective mobile VoIP solution using cellular as they do not see the cost of termination on their bills.

If VoIP is, however, successful then this will mean that the volume of switched terminating minutes subject to price control will decrease. This suggests that expensive structural changes to avoid the need for regulation (such as the imposition of multiple SIM cards and/or the introduction of common, shared or duplicated location registers) will be less likely to pass a regulatory cost benefit analysis. This is because structural changes will involve large fixed costs whilst delivering a smaller overall benefit due to declining volumes.

¹² It should be noted that cellular systems will not support the two way data rates or class-of-service required for VoIP at carrier grade service quality for several years. Even as this position alters, MNOs might use their buyer power over handset vendors to dissuade them from developing and selling dual mode (cellular and wi-fi) handsets and, more directly, use techniques such as Deep Packet Inspection (DPI) to block VoIP calls. For example, we understand one operator in Germany plans to disable calls from the likes of Skype and other VoIP providers, starting in July 2007.

3.2 Regulatory options in the face of SMP (Ofcom Section 4)

Question 5: Do you believe, on balance, that a retail-minus approach to setting wholesale prices could be advantageous?

No. It is unlikely to offer adequate customer protection, to be administratively efficient or to be practical. We think that the likely "spillover effects" would make such regulation detrimental to consumers and consumer welfare overall.

Non-discrimination and price squeeze tests start from the retail price of a service and then deduct the relevant retail costs to arrive at the network charge that the supplier is implicitly "charging itself". Such a test is usually designed to ensure that there is adequate margin in downstream service delivery to allow competition in these (downstream) activities. In this sense, we might agree that it provides "parity" between the wholesale charges and the implicit charge for mobile termination charged in the retail market.

The purpose behind such tests is to encourage service provider competition in downstream markets, but that is not the problem that needs to be addressed here. Rather, the fundamental problem is an absolute one – under current arrangements, only one supplier exists for call termination on an individual network. Lighter regulation in the form of a retail-minus control would not address the underlying issue, because it is designed for another set of circumstances.

In addition, as Ofcom points out, the price squeeze/non discrimination remedy might be expected to have the adverse consequence of diluting MNOs' incentives to compete on the basis of on-net call prices, as any price reduction would benefit rivals (other MNOs and FNOs). The retail-minus approach might therefore encourage competition by means other than lower prices, such as higher commissions for retailers, more competitive advertising and excessive customer churn. Ofcom needs to consider if this is the type of effect it wishes to see for consumers. That is, whether calling parties might instead be better off with fair and reasonable call termination *and* with all operators competing by offering lower prices and/or better mobile calling plans (without their having to consider whether these were also benefiting their competitors).

This remedy would also need either (i) to prohibit MNOs from offering any on-net prices below all the relevant costs or (ii) allow "free/inclusive minutes" but oblige Ofcom to undertake complex computations to work out the implicit charge for call termination in a bundle of services sold by an MNO. This might, in addition, need to be undertaken for each package offered by each MNO. We can therefore only see that the computation of a "retail-minus call termination charge" will start to become ever more complex. This will entail greater administrative cost and provide more scope for disagreement between Ofcom, MNOs and other operators requiring call termination on mobile networks.

Still further additions to the on-going administrative burden would be made by the need to identify "relevant retail costs". Nor it is clear whose costs they should be. The test might be taken for each operator individually or using a hypothetical reasonably efficient operator. But we would ask whether Ofcom

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really wishes to start estimating and monitoring the retail costs either of each MNO or of a hypothetical reasonably efficient mobile operator.

Question 6: Do you agree that asymmetric regulation of voice call termination, which is applied only to termination on 2G networks, will cease to be effective as the proportion of calls terminated on 3G networks grows?

Yes. Clearly, if higher, unregulated rates can be charged on 3G networks then, as the proportion of calls grows, the extent of protection currently afforded to consumers will diminish. Consumers making voice calls to mobiles will pay more, even though they are seeking exactly the same service from the MNOs as previously.

More generally, BT does not understand why the technology behind the delivery of the service is relevant to the regulatory obligations which are deemed to be proportionate, especially as a principle of regulation is that it should be technologically neutral. The reasons for regulation of voice call termination services on 2G networks apply *equally* to 3G networks and we consider that regulation should apply in both circumstances and that this ought to be the *same* regulation. This is one reason why we are in favour of a single price cap which applies to termination on any given MNO network, irrespective of whether the technology used is 2G or 3G.

Question 7: Do you believe that asymmetric regulation of mobile voice call termination, which applies only to termination on 2G networks, will create material incentives to terminate calls on 3G networks? If so, how easily could MNOs develop the technology necessary to follow these incentives?

We do not have a view as to whether MNOs could develop the technology to side-step regulation in the way suggested as a possibility by Ofcom. We are more concerned that Ofcom seems to be envisaging the sanctioning of asymmetric regulation and hence creating the incentives for such "regulatory engineering" in network design (whether this is likely or not). The EC Framework Directive requires NRAs take the "utmost account" of the desirability of making regulation technologically neutral – that is, it does not discriminate in favour of a particular type of technology.

Differences in obligations ought therefore to be related to an assessment of differences in circumstances for customers between any two situations. In terms of the need for consumer protection, assuming the lack of choice for calling parties is equivalent in both situations, then the need for consumer protection is the same in both cases. In this context, we can identify no difference in the situation of a calling party seeking to have a call terminate on a 2G network versus a similar call on a 3G network.

Question 8: Would it be reasonable to require that charges for mobile voice call termination (2G or 3G) are no higher than the cost based charge for the more efficient form of termination? What are the risks and advantages of this approach?

We feel this is putting the cart before the horse as it presumes the regulator knows what is the 'cost based' charge on the different networks. We see, in fact, a number of problems in terms of identifying the "costs" of voice call termination on 3G networks, not least because this will be a cost which is

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shared with a range of new data services to customers. There is a large number of ways in which shared costs can be apportioned between voice and data services and they are likely to provide very different answers as to the 'cost' of voice call termination. Nor is there any one 'right' way to apportion these costs.

Further, to derive costs apportioned on any basis Ofcom will need a forecast of the 'traffic increment' which includes voice services but also the termination of data traffic. In other words, the 'traffic increment' will depend on the uptake of new, 3G services. This forecasting task will therefore be extremely speculative in that it will rely on predictions of demand for new services (which may or may not succeed) in an extremely fast-moving market place in which five years is a very long time.

There will, in short, be huge uncertainty about whether the cost of voice call termination on a 3G network has any meaning or authority. It will basically reflect modelling assumptions made at the outset of the exercise and even then, as a forecast, it will be subject to a very large margin of error. We consider that the statement Ofcom makes in paragraph 4.27 of the *future regulation* consultation, that "[this] can of course be modelled and a conclusion reached which is reasonable across a range of likely scenarios" is very optimistic.

Question 9: On what basis could a single charge control, to apply to both 2G and 3G voice call termination, be calculated?

Given the uncertainties which are certain to prevail about estimating a cost-based charge, for the reasons given in response to Question 8 above we suggest that Ofcom considers what would be a fair and reasonable approach for charges for voice call termination charges. Estimating volumes and making adjustments for deemed inefficiency in the traditional way of setting a price cap does not seem to us to be a suitable approach when one network is being replaced by another and the two networks have different capabilities and can offer a different range of services.

Our suggestion is that, at this time, the costs of the 3G networks are ignored for the setting of voice call termination charges. For the period to 2010, the regulated prices might instead be set on the basis of what would have happened without the implementation of 3G networks – regardless of whether the calls are, in practice, terminated on a 2G network or a 3G network. Ofcom is then presented with a simpler task, as only the updating of an existing model is needed. Consumers would get the same protection as previously and the MNOs would have both the cost of the new networks to fund but at the same time could develop new revenue streams and would not face any extra regulation. That is, the MNOs would both fund the incremental investment but should be allowed to maintain the incremental revenues that will follow from the successful introduction of 3G services. Regulation would still be cost-based, and the situation could be reviewed in 2009 when 3G networks are fully operational and more information will be available about their actual costs (including those for H3G).

In effect, in setting a new charge control, Ofcom needs to estimate the rate of technical progress in mobile voice calls, recalling that the basic property of "X" in an RPI-X formula is that it represents a faster rate of technical progress

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than is being achieved by the economy as a whole. In setting a further price cap, this provides a basic principle which Ofcom might use as a cross-check, given that it shows how much of the innovation in the sector is being passed on to customers of basic call termination.

Question 10: Should mobile termination of mobile originated calls be subject to lighter regulation than mobile termination of fixed network originated calls? If so, what form might that regulation take?

Regulation of fixed call termination services has been justified by the disparity of bargaining power between large and small operators. If this is also a concern in the mobile sector, BT suggests that regulation might also be needed for mobile termination of mobile-originated calls. The most likely manifestation of a problem is the widespread use of on-net call packages whereby MNOs offer rates below those which pass a cost imputation test using non-discriminatory call termination costs (a practice Ofcom noted in paragraph 4.12 of the *future regulation* consultation). This would show that MNOs are not charging their customers what they charge other operators, and will make it much harder for smaller mobile operators to compete. The problem can be avoided if call termination rates are set at a fair and reasonable level in the first place.

Question 11: Is it appropriate for Ofcom to forbear from considering the imposition of regulation on termination of data services?

Yes. BT believes that a general principle of forbearance should be applied to new services. There may be circumstances in which the introduction of new regulations can be justified. However, at the very least, this ought to wait until SMP has been established in a new market and the investing company has both recouped its initial investment and been allowed to keep the benefits from innovation for some time after investments have been recouped. For new 3G services, unless there are unique circumstances which point overwhelmingly to a 'market failure', we do not consider further regulation ought to be considered in the period under consideration (that is, up to 2010).

