



**Effective competition review of
number translation services**

*A statement issued by the
Director General of Telecommunications*

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Summary

S1. Oftel's effective competition reviews are intended to assess the state of competition in a particular sector. In the light of that assessment, Oftel determines the level of regulation appropriate to the amount of competition. This statement presents the findings of Oftel's review of competition in the provision of voice number translation services.

S2. A market which is effectively competitive will deliver the benefits of competition, such as lower prices, higher quality and greater choice of services, without needing sector-specific regulation to promote competition. Regulation is justified when competitive pressures are insufficient to enable consumers to get a good deal in terms of quality, choice and value for money. Under-regulation is not in consumers' interests, but nor is over-regulation, since it can deter investment and hinder innovation.

S3. Number translation services (NTS) are used by their purchasers to provide callers with information or value-added services using non-geographic numbers such as 0800 and 0845, ie numbers which are used to identify a type of service rather than a geographical location. The translation services convert a telephone number from its non-geographic format into a geographic format that enables it to be routed to a specific location. Callers pay a variable charge depending on the type of service being called. The services provided through NTS range from freephone charitable helplines to premium rate information services.

S4. Oftel has conducted this review following a request from BT that Oftel lifts regulatory obligations on BT in respect of certain voice NTS services. Under Condition 43 of its licence, BT is currently required to supply some telecommunications services, including NTS, to any person who reasonably requests such services. Linked to this requirement is an obligation to notify prices and an obligation not to unduly prefer, or discriminate between, customers.

S5. Oftel has taken a number of different factors into account in determining the level of competition in the relevant market, including consumer outcomes, consumer behaviour, market structure and supplier behaviour. Having considered these factors and the matters raised by respondents to Oftel's consultation document, *Effective competition review of number translation services*, published in September 2001, Oftel has concluded that the relevant market for voice NTS is effectively competitive.

S6. A number of considerations have led Oftel to the conclusion that the relevant market is effectively competitive:

- Prices for voice NTS services have fallen in recent years.
- Barriers to entry into the relevant market are low, as evidenced by the extent of entry in recent years. There are now over a hundred potential suppliers of NTS, and the number of suppliers has increased significantly in recent years.
- The costs to customers of switching between NTS suppliers are also low.

- Customers who obtain NTS from operators seem to be well informed about the range of services on offer to them, and are able to use this information to negotiate favourable prices, terms and conditions with suppliers.
- The evidence available suggests BT's market share, which is below 40 per cent, has declined in recent years, whilst the market shares of its competitors have risen.
- Other regulatory measures, including those concerning NTS interconnection, are available to prevent BT from leveraging its market power in related markets into the relevant market for voice NTS.

S7. As Oftel judges the relevant market to be effectively competitive, it does not consider that continued sector-specific regulation in this market is necessary to secure the best deal for consumers. Oftel believes that effective competition will help secure the best possible deal for NTS customers. Oftel therefore intends to consider a determination removing BT's obligation to supply voice NTS services under Condition 43 of its licence, in accordance with the procedure set out in BT's licence. If made, such a determination would also have the effect of removing the obligation to notify prices and the obligation not to unduly prefer or discriminate between customers.

Chapter 1

Introduction

1.1 In January 2000, Oftel published a statement of its strategy, *Achieving the best deal for consumers*. Oftel's strategy is to match the level of regulation to the amount of competition in telecommunications sectors, reducing formal regulation as competition develops, while continuing to protect and inform consumers where effectively competitive markets cannot do so. The aim of market reviews is to assess the level of competition in a particular sector and to ensure that regulation is appropriate to the state of competition. Oftel has published guidelines, *Effective competition review guidelines*, August 2000, which set out how Oftel conducts effective competition reviews.

1.2 Oftel has conducted this market review of Number Translation Services (NTS) following a request from BT that the Director General of Telecommunications (the 'Director') makes a determination under Condition 43 of its licence that BT is not obliged to provide certain voice NTS services on request. BT originally requested that Condition 43 of its licence should not apply in relation to particular voice NTS products it supplies, namely Freefone, Lo-call, Nationalcall, Call Optimiser and Premium Rate Services. The results of this review will therefore be taken into account in assessing BT's request for deregulation in respect of these particular NTS products, and other NTS services in the relevant market.

1.3 The review of the NTS market began in December 2000 with a 'kick-off' statement, *Oftel's 2000/01 review of the NTS market*. Oftel published a consultation document, *Effective competition review of number translation services* ('the consultation document') in September 2001. This statement completes Oftel's market review of voice NTS services.

1.4 This statement sets out:

- detailed descriptions of NTS services;
- an outline of the current regulatory framework;
- conclusions for each indicator used to assess the state of competition;
- final assessment of the state of competition in the voice NTS market; and
- proposals for appropriate regulation of the voice NTS market.

Definition of number translation services

1.5 NTS services are bought by their customers in order to use non-geographic telephone numbers, ie numbers which are used to identify a type of service rather than a geographical location. Services provided through the use of non-geographic numbers include sales, marketing, customer support, and information services. For instance, banks and building societies may use freephone numbers for handling enquiries about financial services. Premium rate services (PRS) numbers, meanwhile, are typically used by service providers to offer content-based services to callers, eg information helplines,

competitions, chatlines, etc. Companies may use a number of different types of NTS. For instance, they may use a freephone number in order to attract new customers, whilst using a local rate number to provide services to existing customers. Internet service providers (ISPs) may also use NTS services in order to provide dial-up Internet access, although NTS services used for non-voice calls are outside the scope of this review. Competition in Internet markets was considered as part of Oftel's review of dial-up Internet access (see *Effective competition review: dial-up Internet access*, January 2002).

1.6 NTS refers to the process associated with the routing of a non-geographic number to a network termination point, eg the translation of a number from its non-geographic format into a geographic number to enable it to be routed to a specific location. In addition to providing the translation services, telecoms operators who supply NTS customers may also provide ancillary services such as analysis of call patterns.

1.7 The NTS customer, or 'called party', is typically an undertaking which uses the non-geographic number in the course of its business. The 'calling party' is the user of the service provided by the called party. The translation services are not therefore supplied directly to the 'calling party', but are instead supplied to NTS customers who use non-geographic numbers to provide services to the 'calling party'.

1.8 There are a number of different types of services which use NTS:

- Freephone: services typically using the 080x/0500 number range. They enable the called party (the NTS customers) to be called free of charge from anywhere in the UK. The NTS customer pays the full cost of the call.
- Local rate: Services typically using the 0845 number range. NTS customers can be called from anywhere in the UK at a price up to the local call rate. The caller pays the local rate and the NTS customer pays the balance. A few NTS suppliers have begun to offer revenue from the calls to NTS customers.
- National rate: Typically using the 0870 number range. Customers can be called from anywhere in the UK at up to the national rate. The caller pays a price up to the full national rate and the NTS customer pays nothing. In some cases, the NTS customer receives some revenue from the supplier of NTS.
- Premium rate service (PRS): Use the 09xx number range. Callers pay for the cost of the call, together with a variable charge for the content of the call. NTS customers earn revenue from the calls.
- Others which limit the cost of calls to a set amount, eg ten pence per minute.

1.9 The use of services that employ non-geographic numbers has grown significantly in recent years, as can be seen from Table One. A significant proportion of the increase is due to rising Internet use (eg the rise in the past few years for freephone calls is largely

due to the growth of unmetered Internet access). The fact that the use of special national rate services (ie calls which use non-geographic numbers and are charged at national call rates) has also increased, however, suggests that the use of services which employ voice NTS (eg services supplied through call centres) has also grown significantly.

**Table One: Fixed line calls using non-geographic numbers
(million minutes per year)**

	1996/97	1997/98	1998/99	1999/00	2000/01
Freephone calls	1,325	2,090	2,305	6,776	34,043
Special local rate	1,219	6,978	20,262	42,799	66,376
Special national rate	492	784	1,410	2,615	3,494
Calls to premium rate services	407	460	888	958	667

Source: *The UK Telecommunications Industry: Market Information 2000/01*, Oftel, December 2001

1.10 It is possible that rising demand for NTS has stimulated a virtuous circle. As demand has grown, new innovative services (eg sophisticated call management techniques) have been offered to NTS customers. For example, a pizza delivery company is making use of NTS services that automatically route a telephone customer's calls to the restaurant nearest to the caller. The availability of such innovative services may have stimulated greater use of NTS services.

The regulatory framework

1.11 Under Condition 43 of its licence, BT is required to supply voice NTS services to any person who reasonably requests such services. Linked to this obligation is a prohibition on undue preference and undue discrimination (Condition 57) together with the requirement to notify prices in Condition 58 (Publication of charges, terms and conditions).

1.12 In contrast, most other operators are only required to supply these services if the Director so determines. Accordingly, unless the Director has made such a determination, those operators are not obliged to provide voice NTS services under Condition 43 of their licences and they are not therefore, subject to undue preference/discrimination or price publication requirements in relation to the provision of voice NTS.

1.13 As a result of its other current regulatory obligations, BT's interconnection retention continues to be regulated. All other operators are free to set their origination and/or termination charges and, through these, the retail prices for calls to their services. The Oftel publication, *Relationship between Interconnection Charges and Retail Prices for Number Translation Services* (published in December 1999) gives more details of the current regulations in the area of NTS interconnection.

1.14 Condition 43 of its licence requires BT to provide services on reasonable request except to the extent that the Director determines otherwise. BT has made a request for such a determination in relation to certain voice NTS services. In considering whether to make a determination under Condition 43.1 to disapply the obligation to supply in relation to those NTS services, the Director is required to have regard to all factors (including those listed in Condition 43.4) which appear to him to be relevant. He must also have regard to his duties under section 3 of the *Telecommunications Act 1984*. If such a determination were to be issued, it would have the effect of removing the obligations on BT not to unduly prefer/discriminate and to notify prices in relation to those NTS services (Conditions 57 and 58 respectively).

Chapter 2

Market definition

2.1 This chapter considers the appropriate market definition for voice NTS services. Defining the relevant market is a first step in assessing the state of competition in the relevant market.

2.2 Oftel's approach to market definition follows that used by the UK competition authorities (see the Competition Act guideline, *Market Definition*) and is in line with those used by EC and US competition authorities. Market boundaries are determined by identifying the constraints on the price-setting behaviour of firms. The two main competitive constraints are the extent to which it is possible for consumers to substitute other services for those in question (demand-side substitution) and the extent to which suppliers could switch, or increase, production capacity to supply the relevant products (supply-side substitution) following a price increase.

2.3 The so-called 'hypothetical monopolist' test is a useful analytical tool for identifying close substitutes in order to set the boundaries of the relevant market. This involves considering whether a hypothetical single supplier of a product could profitably sustain a small, but significant, increase in price for a non-transitory period. If this is not possible, either because of substitution by consumers to a particular product (demand-side substitution), and/or because of a switch in production by suppliers of an alternative product (supply-side substitution), that product is added to the relevant market and the test performed again until a situation is reached where a hypothetical monopolist is able to sustain a small, but significant, non-transitory price increase.

2.4 The geographical boundary of the relevant market is the area within which substitution can take place such that the conditions of competition within that area are broadly similar. If customers can easily purchase from operators located elsewhere, or other suppliers can quickly and cheaply begin to offer services in that area, then the scope of the geographical market needs to include these other areas.

Different types of number translation services

Demand-side substitutability

2.5 Firms generally use different types of NTS for different purposes. Freephone numbers have tended to be associated with sales and marketing applications, whilst firms tend to use local and national rate numbers for longer-term customer service functions.

2.6 This may indicate that businesses regard different types of NTS as part of a portfolio of products, possibly implying that they are complementary rather than being directly substitutable for each other. On the other hand, BT has suggested that since

businesses use the full range of NTS services, their prices will effectively constrain each other. For example, a business could readily shift to using NTS for national rate services in response to a small but significant, non-transitory price increase in NTS for local rate services. Oftel does not have any evidence about customer behaviour in relation to changes in relative prices so it has not been possible to assess the extent of this switching behaviour.

2.7 It is likely, however that PRS calls face different demand-side influences to other types of calls using NTS. Given the different functions and charges associated with PRS, firms may be unlikely to regard NTS for premium rate numbers as close substitutes for other types of NTS. It seems likely that the possibility for demand-side substitution between NTS for PRS and NTS for national rate calls is fairly weak, since premium rate calls are generally used by service providers to generate revenue. Although national rate calls allow service providers to derive some revenue from payments, it does not allow the same scale of revenue that PRS allows. If the price of NTS for PRS were to rise by a small but significant amount, therefore, it seems unlikely that there would be a large-scale shift by NTS customers to NTS for national rate calls, for example.

Supply-side substitutability

2.8 In contrast to the possibility for demand-side substitution, there is considerably more scope for supply-side substitution in response to a small but significant, non-transitory increase in the price of one category of NTS. For example, if a hypothetical monopolist supplier of local rate NTS increased the price of its services it seems likely that operators providing freephone, national call rate or PRS would be able to quickly switch into supplying NTS for local rate calls without having to make substantial additional investments. Once an operator has established the intelligent network platform to terminate NTS calls, it can be used equally for all types of NTS voice calls. In addition, the marketing and distribution systems for the various types of NTS are likely to be very similar. In support of this view, Oftel observes that it is fairly commonplace for terminating operators to offer the full range of NTS services. This provides some evidence of the ability of operators to practise supply-side substitution.

Geographical market

2.9 It seems clear to Oftel that the relevant geographical market is national. As noted in Oftel's statement, *Tariffing Issues: Bundling of Inbound and Outbound Services* (October 1998), an operator does not require a national network in order to provide the NTS call termination services to businesses across the UK; it is sufficient for operators to be able to interconnect with the networks of BT and other operators to provide a national service.

Voice and data markets

2.10 Oftel believes that the relevant market for NTS should encompass voice services only. Oftel considers that there is a distinct market for NTS for data services. This issue has been considered with reference to the hypothetical monopolist test. If a sole supplier of NTS for data services increased the price by a small but significant amount (for a non-transitory period of time) it seems unlikely that NTS customers would find NTS for a voice telephony service to be an effective substitute. This conclusion reflects the fact that callers are currently limited in their ability to substitute voice telephony for data services.

2.11 The possibility of supply-side substitution also needs to be considered, however. Internet traffic is increasingly moving away from using traditional NTS services through digital local exchange (DLE) connection. This is outside the scope of this review and it should also be noted that competition in Internet markets was considered as part of Oftel's review of dial-up Internet access (see *Effective competition review: dial-up Internet access*, January 2002).

2.12 However, to the extent that data still uses the traditional NTS route, supply-side substitution between use of NTS for voice and for data could be relevant, although it only appears to be possible for large players as smaller NTS operators do not always possess the necessary call termination exchanges capable of terminating ISP calls. Nonetheless, supply-side substitution by larger players alone could in theory be sufficient to maintain a common pricing constraint between NTS services used for voice and data calls. At present, Oftel does not have conclusive evidence as to the extent to which such a constraint operates in practice, especially given the recent shift of data traffic away from traditional NTS services.

2.13 Although there is the possibility of some supply-side substitution therefore, the scope for demand-side substitution is more limited. In the light of this, Oftel has adopted as the relevant product market for the purposes of this review the supply of NTS used for a voice telephony service.

Services additional to NTS

2.14 Some of the larger NTS suppliers, including BT, offer other facilities, such as statistical analysis of call patterns, in addition to translation services themselves. But Oftel believes that these firms operate in the same economic market for NTS as those who offer a more basic NTS package since the prices of the translation services themselves are constrained by the availability of similar services from elsewhere.

Relevant market: summary

2.15 Respondents to the consultation document agreed that the relevant market should be defined as the one for NTS used for voice calls. One respondent suggested that the different types of voice NTS services (eg local rate, national rate etc) may be in separate markets. Oftel considers the different types of voice NTS services to be within the same market because of the possibility of supply-substitution, and also because

some demand-side substitution is also likely to be possible. The fact that suppliers of one type of NTS for voice traffic can readily supply other types of NTS has led Oftel to include these different types of NTS within the relevant market. There is also the possibility of some demand-side substitution between different types of voice NTS. For the purposes of this review, therefore, Oftel has used the market definition of the supply in the UK of NTS for a voice telephony service.

Chapter 3

Indicators of effective competition

3.1 Oftel's guidelines, *Implementing Oftel's strategy: Effective competition review guidelines*, set out four groups of indicators of effective competition: consumer outcomes; consumer behaviour; market structure; and supplier behaviour. The consultation document, *Effective competition review of number translation services*, published in September 2001, set out Oftel's view on each group of these indicators. This chapter summarises Oftel's final conclusions for each of these indicators and on the state of overall competition in the market.

3.2 For the purposes of this review, the 'consumers' of NTS are the companies or individuals that use NTS in order to provide callers with services using non-geographic numbers. They are referred to as NTS customers. References to consumers, and consumer outcomes, should be considered as references to NTS customers rather than end users.

Consumer outcomes

A wide range of services

3.3 Alongside translation services, NTS suppliers also offer facilities which allow sophisticated management of calls, such as the ability to match callers with suitably qualified call handlers. Some operators are even integrating the provision of NTS with the facilities to handle the calls themselves (eg call centres). In its response, BT provided evidence that indicated that a significant number of its competitors are able to offer a full range of these additional facilities.

Consumer behaviour

Consumers able to access and use information

3.4 NTS customers are often companies with a commercial imperative to obtain services at the lowest possible cost. This makes it more likely that they will be able to take advantage of market opportunities. Some NTS customers, for instance, issue invitations to tender which allow them to compare the prices and services offered by different potential suppliers of NTS.

3.5 The benefits of competition are not only derived by larger operators. Some small- and medium-sized enterprises enter into joint purchasing agreements which allow them to gain better terms and conditions than otherwise possible - although Oftel understands the number of these to be currently limited.

3.6 In its response to the consultation document, BT provided evidence that a number of different NTS customers obtain services from more than one supplier, using one NTS

supplier for local rate services, for example, and a different one for national rate services. Such purchasing behaviour could allow customers to readily compare the prices and quality of service offered by different NTS suppliers, and thereby make it more likely that NTS customers are in a position to negotiate better deals with suppliers. Oftel considers that such strategic purchasing behaviour provides evidence to show that NTS customers are able to make effective choices, which, in turn, makes it unlikely that any supplier of NTS will be able to exercise any market power.

Absence of barriers to consumers switching suppliers

3.7 If NTS customers faced significant costs in switching from one supplier to another, then this could inhibit competition and confer market power on one or more operators. One possible significant switching cost could arise from the fact that NTS customers may spend considerable sums in promoting particular telephone numbers to callers. This spending may then deter them from switching between NTS operators if that involved changing telephone numbers.

3.8 For a number of years, however, it has been possible for NTS customers to switch between different suppliers whilst keeping the same telephone numbers as previously. Number portability has thus meant that switching costs for NTS customers are low. There may however be some other costs associated with switching suppliers. For instance, the transaction costs in finding, and negotiating with, alternative suppliers. Alternatively, there may be barriers to switching if NTS customers are tied to lengthy contracts. The practice of inviting NTS suppliers to tender for a contract would appear to keep transactions costs low, however, whilst the practice used by some NTS operators of buying customers out of their existing supply contracts may also mean that the length of supply contracts does not prevent switching between suppliers.

3.9 As indicated in the consultation document, the extent to which NTS customers have been prepared to switch from BT to other NTS suppliers provides an indication that there are low barriers to consumers switching suppliers. The figures provided to Oftel by BT demonstrated that the proportion of its numbers that had been ported to other NTS suppliers increased from 3.33 per cent in 1997-98 to 17.67 per cent in 2000-01.

Market structure

Changes in market structure over time

3.10 There has been a significant degree of entry into the NTS market in recent years. Over 180 companies have blocks of numbers which can be used to provide NTS, and Oftel understands most, but not all, of these companies are actively supplying NTS. Figures provided by BT have indicated that the number of other licensed operators (OLOs) terminating NTS calls originated on the BT network rose by over 50 per cent (from 61 to 94) between March 1999 and December 2000. It is possible that this number underestimates the total number of NTS suppliers because it does not include information from other originating operators.

Market shares

3.11 As discussed in Chapter two, Oftel believes that the relevant market includes all the various types of voice NTS services. Before publishing the consultation document, Oftel sought market information from different NTS suppliers. It was not, however, possible to derive a complete set of market share figures because of the large number of different NTS suppliers and because of difficulties in separating voice traffic which used NTS from similar data traffic. Oftel's previous consideration of competition in the NTS market (see the 1998 statement, *Tariffing Issues: Bundling of Inbound and Outbound Services*) used figures for NTS traffic carried over BT's network as indicators of market shares. A similar approach was used in the consultation document to derive a figure for BT's market share, although Oftel acknowledged that the data excluded calls originated on non-BT networks and did not incorporate the effects of number portability, which lead some non-geographic calls to be terminated by an operator other than the one to whom a particular number is allocated.

3.12 The figures provided by BT, and published in the consultation document, indicated that its market share was around a third of all voice NTS calls. BT has since provided more up-to-date figures for its market share but has asked that the precise figure be withheld for reasons of commercial confidentiality. BT's share in the market for voice NTS services is not at a level which would normally be taken to indicate individual dominance, which would be indicated by the ability of a firm to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers. The Competition Act guidelines, *The application in the telecommunications sector*, March 2000, state that it is "unlikely that an undertaking will be dominant individually if its market share is below 40 per cent."

Limited entry barriers

3.13 The extent to which the behaviour of undertakings in a particular market is constrained by the threat of entry from other undertakings is an important factor in assessing the state of competition. If entry barriers are low, then the incumbent firms will be constrained by the prospect of entry from new firms and are thus unlikely to possess market power.

3.14 Oftel considers the relevant market for voice NTS services to have low entry barriers. There are two main ways of entering the market. One is through acquiring a licence to provide NTS and investing in the necessary infrastructure; the second is to become a reseller of NTS. The availability of this second method means that the sunk costs of entering the market are particularly low. Where the first method is pursued there would have to be some investment in hardware and software, but the costs involved are not such that they would be expected to constitute a significant barrier to entry. The technology used to offer NTS is relatively commonplace, for instance, and is often embedded in the switches used by network operators.

3.15 Not all of the firms with NTS number codes allocated to them are currently active in the market. But if they were to become aware of profitable opportunities available (ie if prices for NTS were to be raised consistently above the competitive level by one or more operators) many of them could enter the market relatively easily. This fact is likely to restrain the pricing behaviour of the firms currently supplying NTS to customers

3.16 The rise in the number of operators in the relevant market for NTS seems to indicate that the barriers to entry into the market are low. As discussed in the consultation document, the number of operators offering NTS services increased by over 50 per cent between March 1999 and December 2000. Other things being equal, entry will be more likely in a growing market than in one which is static or declining. The fact that the NTS market has been growing rapidly is thus likely to have facilitated entry.

Potential for the leverage of market power

3.17 Although BT has market power in a number of separate telephony markets, it is subject to regulatory obligations which prevent it from leveraging this market power into the market for NTS. For instance, the terms offered by BT for interconnection for NTS calls continue to be regulated in order to prevent the leverage of market power from call origination.

3.18 Some respondents argued that it was necessary to continue regulation of BT's retail provision of NTS services as a result of its position in the market for call origination. It was argued that the obligation to publish prices under Condition 58 of the BT licence, assisted in regulation of NTS interconnection because it created greater transparency about whether the prices offered by BT for interconnection were anti-competitive or not. Oftel does not consider it necessary to retain price publication obligations solely to put into effect regulation of interconnection arrangements since it would be possible for Oftel to use its statutory powers to obtain the necessary information even after regulation in the retail market has been removed.

3.19 Some respondents also argued that Oftel's current regulatory regime for NTS interconnection had not been sufficient to prevent what was claimed to be anti-competitive behaviour on the part of BT, and that, as a result, continued regulation of the retail provision of NTS was also necessary. Oftel has considered this argument, but believes that the possibility of leverage of market power can be prevented through application of the existing regulations concerning interconnection. The maintenance of regulation in the retail provision of voice NTS is not necessary and would not be a proportionate means of addressing the issue of the existence of market power in related markets which are themselves the subject of regulation.

Supplier behaviour

Active competition on price and quality

3.20 The large number of suppliers in the market for voice NTS, each of which offers a number of different types of service, means that NTS customers are in a position to choose an NTS product which is tailored to their individual needs. For instance, most NTS suppliers offer significant volume discounts which also leads to a wide variety of different pricing options.

3.21 Growing competition in the market seems to have led to a fall in prices for NTS customers. Due to the large number of suppliers, and the fact that pricing tends to be bespoke, it is not possible to provide a complete picture of how prices in the market have fallen. The fact that BT's published prices have declined significantly since 1995 (when number portability was introduced) demonstrate however that increasing competition has had an effect. As indicated in the consultation document, the amount charged by BT for local rate NTS, for instance, has fallen by approximately 50 per cent since 1995.

3.22 It is also notable that some NTS suppliers are giving service provider payments for national rate calls and local rate calls whereas in the past these have been restricted to premium rate services. In recent years, the level of payments to service providers for national rate and premium rate calls has also increased, suggesting that price competition in those areas is also common.

3.23 The price charged for NTS is only one of the factors in assessing the state of competition. As indicated above, there is a wide range of services offered by different suppliers, including tailor-made packages with features such as call management, call routing and call information. As lower switching costs have stimulated competition in prices, they are also likely to have increased competition in terms of quality of service and range of additional services offered.

Profitability

3.24 Profitability levels may demonstrate market power alongside other indicators of market power, notably market share and low entry barriers. In a competitive market, Oftel would expect prices, and consequently profits, to broadly reflect efficiently incurred costs plus an adequate return on capital. In this particular case, Oftel has not regarded it as proportionate to seek to obtain evidence on the profitability of supplying NTS. The other signs of effective competition, such as low barriers to entry, falling prices and BT's declining market share, provide sufficient evidence that competition in the market is effective.

Absence of anti-competitive behaviour

3.25 Oftel has not substantiated any complaints and representations relating to BT's behaviour in the provision of translation services to NTS customers.

Absence of collusion

3.26 It is possible that the current regulatory obligation on BT to publish prices may lead to muted competition between NTS suppliers. Since it is currently obliged to publish its prices in advance, it is possible that other companies may use these as a marker to set their own prices. Oftel has examined whether price publication obligations dampen competition by encouraging price following. The statement, *BT's regulatory obligations to provide advance notification of price changes and to maintain a published price list*, (March 2002), discusses the issue of price publication obligations in more detail and sets out proposals for reducing the period of advance notification on a trial basis.

3.27 Outright price collusion is unlikely in Oftel's view to be a feature of the market for voice NTS services. Such collusion is more likely when the number of firms in an industry is small and when prices in the market are readily visible. Given that negotiations over prices for NTS tend to be undertaken on an individual basis, and that there are over a hundred suppliers in the industry, it is unlikely that collusion is a feature of this market. These factors also suggest that signalling of prices, often associated with tacit price collusion, is unlikely in the provision of NTS. The fact that prices have declined in recent years, rather than remained stable for long periods, provides further evidence for the conclusion that tacit or explicit price collusion does not appear to be taking place.

Conclusion

3.28 On the basis of the evidence considered before publication of the consultation document and the evidence provided by respondents, Oftel has concluded that the relevant market for NTS is effectively competitive. A number of different considerations have led Oftel to this conclusion:

- Prices for voice NTS services have fallen in recent years.
- Barriers to entry into the relevant market are low, as evidenced by the extent of entry in recent years. There are now over a hundred potential suppliers of NTS, and the number of suppliers has increased significantly in recent years.
- The costs to customers of switching between NTS suppliers are also low.
- Customers who obtain NTS from operators seem to be well informed about the range of services on offer to them, and are able to use this information to negotiate favourable prices, terms and conditions with suppliers.
- The evidence available suggests BT's market share, which is below 40 per cent, has declined in the past few years, whilst the market shares of its competitors has risen.
- Other regulatory measures, including those concerning NTS interconnection, are available to prevent BT from leveraging its market power in related markets into the relevant market for NTS.

Chapter 4

Appropriate regulation

4.1 This chapter sets out Oftel's views on the appropriate level of regulation for the NTS sector given the conclusion that the NTS sector is effectively competitive. Oftel's strategy provides a framework to ensure appropriate regulation is achieved, adjusted to the level of competition in the market and focused on the area of concern. Too much, or too little regulation can work against consumers' interests by deterring investment and innovation. Given that the market for NTS appears to be effectively competitive, removal of the current regulatory obligations on BT would appear to be appropriate and Oftel will commence a consultation on this as discussed below.

4.2 Some respondents argued that the market outcomes outlined in the previous chapter have happened because of BT's current regulatory obligations; the implication being that the indications of growing competition in the market for voice NTS would be put at risk if BT's current regulatory obligations were lifted. Oftel considers that the observed signs of growing competition are the result of entry into the industry, and regulation (notably the advent of number portability) has played a role in lowering entry barriers. Oftel does not consider that removal of existing regulation would lead to a significant raising of these barriers. It should also be noted that if BT's current regulatory obligations were removed, the Director would, if appropriate, impose such obligations as were necessary to fulfil his statutory duties.

4.3 New EC Directives will come into force shortly and will require Oftel to undertake a series of market reviews to assess whether regulatory obligations currently in place remain appropriate. In most cases, regulation would only be appropriate in markets that were not effectively competitive, ie where one or more operators have 'Significant Market Power' (SMP), with SMP defined such that it is equivalent to the competition law concept of dominance. Further details of the impact of the new EU directives are set out in *Draft Oftel Management Plan 2002/3* (December 2001).

4.4 One respondent suggested that Oftel should not lift the existing regulation until it had evaluated the costs and benefits of removing the current regulation. Oftel considers that if effective competition is present in a market then it is not normally necessary to maintain ex ante regulation. Oftel's strategy statement, (*Achieving the best deal for consumers*, January 2000) indicates that where competition is effective, it is not necessary to evaluate the costs and benefits of sector-specific regulation before it is removed.

4.5 A respondent also suggested that there is no requirement on Oftel to remove the existing regulatory obligations on BT if it concludes that the market is effectively competitive. Oftel has stated in its strategy statement, *Achieving the best deal for consumers* (January 2000), that it will keep regulation to the minimum necessary to obtain appropriate outcomes. Oftel believes that ex ante regulation is justified when competitive pressures are insufficient to enable consumers to get the best possible deal

in terms of quality, choice and value for money. Unjustified regulation can deter investment and hinder innovation.

4.6 The Director's current view is that all reasonable demands for voice NTS will be met by effective competition in the market. The Director therefore intends to consider removing the obligation on BT in accordance with Condition 43.4 of the BT licence. The Director intends to issue a notice to BT and interested parties for consultation on the proposal to determine that BT's obligation to supply voice NTS services under Condition 43 of its licence should be disapplied. The issue of the notice will be the commencement of the procedure set out in paragraph 6 of Part I of Schedule I of BT's licence. BT and interested parties will have 28 days to comment. This will be followed by a further 28-day period to allow BT and interested parties to make observations on the published representations. At the end of the second 28-day period, having considered all representations and observations, the Director will, if appropriate, publish a draft determination. BT and interested parties will have a further 14-day period to comment on the draft determination. The Director will consider all comments and inform BT and interested parties of his final decision after the end of that period.

Scope of the determination

4.7 The consultation document asked whether any future determination lifting regulation should be focused on BT's current voice NTS services (including the products for which it had specifically asked the current regulations to be lifted), or whether it should cover all voice NTS services, including any such services launched by BT in the future. Having considered the responses, Oftel currently believes that any such deregulation should apply to all services in the market which has been found to be effectively competitive, ie NTS services used for a voice telephony service. This will be considered further in the forthcoming consultation.

Annex A: Responses

Oftel received responses to its consultation document from the following organisations (listed in alphabetical order):

- BT
- Cable & Wireless
- Directline
- Energis
- NIACT
- Telephone Helplines Association
- Thus

Annex B: Glossary

Barriers to entry – an additional cost which must be borne by entrants but not by firms already in the industry; or other factors, which enable an incumbent to maintain prices above the competitive level without inducing entry.

BT - British Telecommunications plc.

Interconnection – the physical and logical linking of telecommunications networks used by the same or a different organisation in order to allow the users of one organisation to communicate with users of the same or another organisation, or to access services provided by another organisation. Services may be provided by the parties involved or other parties who have access to the network.

Internet service provider (ISP) – a service provider who provides access to Internet services

Market power – the ability to profitably raise prices above the competitive level for a non-transitory period.

Non-geographic number - these are numbers which are used to identify a type of service rather than a geographical location. These services are sometimes referred to as Specially Tariffed Services and include freephone, local rate, national rate and premium rate numbers. Mobile and Personal numbers are also non-geographic numbers.

Number portability – number portability between operators enables a customer to transfer from one operator to a second operator and retain the same number provided the customer remains at the same address.

Number Translation Services (NTS) - the process associated with the routing of a non-geographic number to a network termination point, eg the number is translated from its non-geographic format into a geographic number to enable it to be routed to a specific location.

Other Licensed Operators (OLO) - companies, other than BT, which operate telecommunications systems.

Premium Rate Service (PRS) – services, including recorded information and live conversation, run by independent service providers. All calls to these companies are charged at a higher rate than ordinary calls to cover the companies' costs in providing the content of the call and the operator's cost for the special network facilities needed.

Voice telephony service – a service available to the public for the commercial provision of direct transport of real-time speech via the public switched network or networks such that any user can use equipment connected to a network termination

point at a fixed location to communicate with another user of equipment connected to another termination point.