

**Draft Direction under the provisions of Regulation 6(6) of the
Telecommunications (Interconnection) Regulations 1997 to
resolve a dispute between Telewest and BT over interconnect
charges for origination of calls to freephone numbers**

26 June 2002

Contents

Draft Direction

Chapter 1 Summary

Chapter 2 Background

Chapter 3 History of the dispute

Chapter 4 The arguments made by the parties

Chapter 5 The Director's decision and reasons

Chapter 6 Consultation and timetable for responses

Annex A Schedule of operators in the Telewest Group of Companies

DRAFT DIRECTION UNDER THE PROVISIONS OF REGULATION 6(6) OF THE TELECOMMUNICATIONS (INTERCONNECTION) REGULATIONS 1997 OF A DISPUTE BETWEEN TELEWEST COMMUNICATIONS PLC AND OTHER OPERATORS IN THE TELEWEST GROUP OF COMPANIES AS SET OUT IN ANNEX A TO THIS DRAFT DIRECTION (“TELEWEST”) AND BRITISH TELECOMMUNICATIONS PLC (“BT”) OVER INTERCONNECT CHARGES FOR ORIGINATION OF CALLS TO FREEPHONE NUMBERS

WHEREAS:

- A. The Secretary of State granted to British Telecommunications on 22 June 1984 a licence (the “BT licence”) under section 7 of the Telecommunications Act 1984 (“the Act”) for the running of telecommunications systems specified in that Licence;
 - B. By virtue of section 109 of paragraph 20 of Schedule 5 of the Act the BT licence has effect as if granted to British Telecommunications plc (“BT”);
 - C. The Secretary of State has granted to Telewest Communications plc and the other operators in the Telewest group of companies as set out in Annex A to the draft direction on 14 January 1997 licences under Section 7 of the Act for the running of a telecommunications system as specified in the licence;
 - D. On 1 January 1998 the Interconnection Directive came into force and was implemented in the UK through the Telecommunications (Interconnection) Regulations 1997 (the “Regulations”) and conditions in the licences of operators;
 - E. Regulation 6(6) of the Regulations provides that where there is a dispute concerning interconnection between organisations, the Director General of Telecommunications (“the Director”) shall, at the request of either party, take steps to resolve the dispute within six months of the date of the request. The Determination which the Director makes to resolve the dispute must represent a fair balance between the legitimate interests of the parties, and must be notified to the parties in accordance with Regulation 8(3). The parties are entitled to a full statement of the reasons on which the Determination is based;
 - F. Telewest entered into an Interconnect Agreement with BT on 20 October 1997;
 - G. On 23 November 2001, Telewest issued an Operator Charge Change Notice (“OCCN”) to BT. The OCCN sought an increase in the call origination charges payable to Telewest by BT for Freephone traffic terminating on the BT network;
 - H. On 3 December 2001, BT rejected Telewest’s OCCN on the basis that it did not conform to the current NTS formula as determined by Oftel. Telewest and BT are unable to agree on this matter and are therefore in dispute;
-

- I. On 14 February 2002, in accordance with the provisions of Regulation 6(6) of the Regulations, Telewest referred this dispute to the Director for determination;
- J. The Director has a duty to encourage and secure adequate interconnection in the interests of all users in a way which provides maximum economic efficiency and gives maximum benefit to end-users;
- K. The Director has considered, inter alia, the information provided by the parties and the matters set out in Regulation 6(8) of the Regulations. The principal points are summarised in the Explanatory Memorandum which accompanies, and is published with, this Direction;
- L. A draft of this Direction and the Explanatory Memorandum was issued to interested parties on []. Comments were invited by [];

NOW, THEREFORE:

PURSUANT TO REGULATION 6(6) OF THE INTERCONNECTION REGULATIONS, AND HAVING CONSIDERED THE VIEWS OF THE PARTIES AND THOSE MATTERS SET OUT IN REGULATION 6(8) OF THOSE REGULATIONS, THE DIRECTOR MAKES THE FOLLOWING DIRECTION TO RESOLVE THE DISPUTE BETWEEN TELEWEST AND BT:

1. Telewest may propose its own price for the charge of originating a Freephone call that originates on Telewest's network and terminates on BT's network.
2. The terms defined in this direction shall have the meaning so defined or described. All other words or expressions used in this direction shall have the same meaning as in the Directive, the Regulations, the Act or the Licence as appropriate.
3. This direction shall take effect on the date it is published.

Chris Kenny
Director of Compliance

**A person authorised under paragraph 8 of Schedule 1 of the
Telecommunications Act 1984**

[Date]

Chapter 1

Summary

1.1 The Director General of Telecommunications (the 'Director') has issued a draft Direction in accordance with the provisions of Regulation 6(6) of the Telecommunications (Interconnection) Regulations 1997 (the 'Regulations') for the resolution of a dispute between Telewest plc and other operators in the Telewest group of companies as set out in Annex A to this draft direction ('Telewest') and British Telecommunications PLC ('BT').

1.2 Telewest referred this dispute to the Director on 14 February 2002. Argument submitted on this issue by Telewest and BT is set out in Chapter 4. The Director has considered the submissions made by Telewest and BT, and has issued this draft Direction in respect of the dispute. Comments are requested and will be taken into account in making a final Direction.

1.3 Telewest requested a determination from the Director that:

- Telewest should be able to set its own price for the charge of a Freephone call which originates on Telewest's network and terminates on BT's network; and
- any such charge should be derived from a reasonable Telewest specific-cost estimate.

1.4 Therefore, Telewest is seeking a determination by the Director on an issue of principle. The principle in question is whether Telewest should, in the context of the current NTS regime and the Standard Interconnect Agreement (SIA), be allowed to issue an OCCN on BT which proposes Telewest's own call origination charges.

1.5 The details of the Director's consideration of the submissions made by Telewest and BT, together with the reasons why the Director is minded to make this draft direction, are set out in Chapter 5.

1.6 In summary, the Director is minded to direct that Telewest should be able to propose its own price via an Operator Charge Change Notice (OCCN) for the charge of a freephone call which originates on its network and terminates on BT's network. The OCCN process is set out in 2.14. The Director does not consider that Telewest is in a position to enforce an unreasonable charge. As neither party to the dispute holds a position of market power in the relevant market, a reasonable charge will be achieved via negotiations between the parties. Therefore the Director is resolving this dispute by allowing Telewest to propose its own charge, as any charge consequently negotiated will be reasonable.

1.7 Furthermore, the Director considers that Telewest, and originating operators other than BT, should be able to set in place their own arrangements for originating freephone calls that terminate on all other networks, not just BT's. Without fettering the Director's discretion to take a different view in the light of circumstances, if a similar dispute was referred to Oftel in the future, the Director's current view is that the outcome would be similar to the one that has been reached in the present dispute.

1.8 Having considered the facts specific to this dispute and the matters set out in Regulation 6(8) of the Regulations, this draft Direction, in the opinion of the Director, represents a fair balance between the interests of the parties in each case, having regard to the Director's wider duties to promote the development of the telecommunications industry in the UK and to encourage and secure adequate interconnection in the interests of all users in a way that provides maximum economic efficiency and gives the maximum benefit to end users.

Chapter 2

Background

Call origination

2.1 The originating network is the network with access to the customer who makes a call.

Call termination

2.2 The terminating network is the network to which a customer who receives a call is directly connected.

2.3 Call termination of a geographic call has particular characteristics that arise from the call termination externality. An externality may be said to exist where the actions of an individual or organisation cause costs to be incurred by others (or benefits to be gained by others), but that the individual or organisation has no incentive to take such effects into account.

2.4 The externality in the termination of geographic calls arises because the retail price of a call is paid by the caller, not the call recipient. This is known as the 'calling party pays' principle. The price of call termination depends on the network that the receiving party resides on and the caller has no control over this. Consequently there is likely to be market power in call termination of a geographic call.

Description of Number Translation Services (NTS)

2.5 The term NTS describes a range of specially non-geographic tariffed services, primarily used for telemarketing, which include freephone calls, 0845 Access (LCFA) and 0870 (NCFA). NTS calls are different from geographic calls, because the caller is generally accessing a service at the other end of the call.

New NTS

2.6 In December 1999, OfTel published its *Statement on the relationship between interconnection charges and retail prices for Number Translation Services* (the 'NTS statement') (see www.oftel.gov.uk/publications/1999/pricing/nts1299.htm). The NTS statement followed a lengthy discussion and consultation exercise in response to a general industry view that the then existing NTS formula constrained the ability of terminating operators to exercise sufficient control over their NTS revenues.

2.7 The new regime was intended to give terminating operators sufficient flexibility in order that they could establish the price at which they would be remunerated for

NTS calls. This price would then be added to BT's regulated call origination charge plus any transit charges to establish the retail price for their service.

2.8 The NTS statement confirmed that that these arrangements do not apply to originating operators other than BT. Paragraph S.4 of the NTS statement stated the following:

*“These arrangements do **not** apply to originating operators other than BT. These operators are free to set their own originating charges and it is up to them to negotiate with terminating operators the payments required for access to their services”.*

Freephone calls

2.9 As indicated in paragraph 2.5, a freephone call is an NTS service. For freephone calls, the called party pays the charge, including the charge for the call origination service that is provided by the originating operator. For other NTS calls, the calling party pays the charge for originating the call.

2.10 In light of the fact that the called party pays the charge for originating a freephone call, it has to be considered whether the externality that exists in the termination of a geographic call is present in the case of freephone call origination. If the competitive conditions in freephone call origination are sufficiently similar to those in call termination for a geographic call, then the externality may also be present in freephone call origination, and the operator originating freephone calls might possess market power. However, if call origination for freephone calls has the same characteristics as call origination generally, operators originating freephone calls (apart from BT) would not possess market power.

2.11 The Director considers that this issue is a key factor that will need to be carefully considered for the purposes of considering Telewest's determination request. This issue will be analysed in Chapter 5.

Reciprocity

2.12 The reciprocity principle states that for services that are provided reciprocally, charges should also be reciprocal. The Director supports the principle of reciprocity for the termination of geographic calls, as it is the calling party and not the called party that pays for call termination, thus creating diminishing incentives for terminating operators to reduce the cost of terminating a call on their network. Higher costs are likely to be passed on to retail customers. Therefore reciprocity minimises the distorting effects of this externality.

2.13 As set out in paragraph 2.10, if the origination of a freephone call is sufficiently similar to the termination of a geographic call, this might place the operator originating the freephone call in a position of market power. If this was the case, the arguments for reciprocity that are relevant in the context of geographic

call termination might also apply to the origination of freephone calls by originating operators other than BT.

The OCCN process

2.14 Clause 13 of BT's SIA describes the process used by Operators, including BT, for offering and amending charges in payment for access to another Operator's services. For example, where an originating operator proposes to change the price paid to the terminating operator for terminating calls, it issues an Operator Charge Change Notice (OCCN) to the terminating operator. The operator receiving the OCCN has 14 days to decide whether to accept or reject the new charge and to notify the originator of the OCCN. Failure to notify within 14 days signals a rejection of the proposal. Where the proposal is rejected, both operators have a further 14 days to settle the resultant dispute. If after this second period the dispute remains unsettled, either operator may refer the dispute to the Director.

Chapter 3

History of the dispute

3.1 On 23 November 2001 Telewest issued an OCCN to BT. The OCCN sought an increase in the call origination charges payable to Telewest by BT for Freephone traffic terminating on the BT network.

3.2 For the purposes of the OCCN, Telewest calculated that 18% of Telewest originated freephone calls involve a tandem leg before delivery to BT. Thus a factor of 18% of double tandem short was added to the existing BT single tandem rate to produce a Telewest specific figure.

3.3 On 3 December 2001, BT rejected Telewest's OCCN. The explanation given by BT for rejection of this OCCN was that:

"BT rejects this proposed charge change, which applies to a BT charge, because it does not conform to the current NTS formula as determined by OfTel".

3.4 Telewest referred this dispute to the Director in a letter of 14 February 2002. In this letter, Telewest stated that the dispute with BT concerned Telewest's ability to set its own call origination charge under the SIA with BT, with the aim of recovering its justifiable and reasonable costs in originating freephone calls to BT.

3.5 Telewest further stated that it should be able to set its own price for the charge of originating a call on Telewest's network, and that any such charge should be derived from a reasonable Telewest specific-cost estimate.

3.6 Telewest sought a determination from the Director on whether Telewest should, in the context of the current NTS regime and the SIA, be allowed to issue an OCCN on BT which sets Telewest's own call origination charges.

Information sought by the Director

3.7 The Director provided BT with a copy of Telewest's letter of 14 February 2002. In a letter of 8 March, the Director asked BT to provide a more detailed explanation of why the Telewest OCCN of 23 November 2001 was rejected. The Director requested that this elaboration should explicitly state the aspects of the current NTS regime that BT considers Telewest's request infringes. BT responded to this request in a letter of 22 March.

3.8 BT's letter of 22 March was copied to Telewest, who subsequently responded to the points BT made in a letter of 18 April. Telewest's letter of 18 April was also copied to BT.

3.9 In a letter of 7 March, the Director asked Telewest to provide further information on the analysis that Telewest undertook for the purposes of the

OCCN. In a letter of 30 April, the Director asked Telewest to provide details of the routing analysis that it had undertaken in order to determine that 18% of freephone calls involved a tandem leg within the Telewest network before being delivered to BT. Telewest responded to this request in a letter of 7 May 2002. Telewest requested that this response be treated as confidential to Oftel.

Chapter 4

Arguments made by the parties

Telewest's letter of 14 February 2002

4.1 Telewest considers that it has fully supported moves towards cost orientation, and that it was one of the few operators to accept BT's proposal to use INCA as the basis for NTS interconnect charges – in spite of the consequent increase in BT's originating retention. Furthermore, Telewest refers to the INCA Direction of 20 December 2001, where it is noted at paragraph 2.5 that:

“At the time of the [original] NTS Determination it was acknowledged that BT's origination and conveyance charges to different operators would vary according to the amount of its network that was used”.

4.2 Telewest argues it was further recognised that these charges would vary on a call-by-call basis, and that a mechanism should be put in place to measure costs accordingly.

4.3 Telewest states that under the current NTS regime, it receives BT's single tandem charge – uplifted by relevant retail costs – for originating all NTS traffic that terminates on the BT network. Telewest states that this charge is inappropriate.

4.4 Telewest believes that it should ultimately be able to set all origination and termination charges on an operator specific basis, to reflect Telewest's own cost structure in relation to network resource used and appropriate retail costs.

4.5 Telewest states that the methodology which it applied to set its own origination charge for the purposes of the 23 November OCCN is essentially identical to that adopted by multi-switch operators under the PSTN 'reciprocity' regime for call termination. Telewest considers that this is one justifiable cost-based way of setting its own origination charges. Telewest further states that in the future it would expect to derive more detailed methodologies to produce appropriate estimates of its own costs, for example, on an annual basis.

BT's letter of 22 March 2002

4.6 BT considers that it is in a different position from other originating operators, as its retention is heavily regulated as a result of Oftel's determination that BT is dominant in that market. BT argues that it must fully cover its costs with regard to call origination.

4.7 BT contrasts its position in call origination with that of Telewest. BT argues that Telewest has no requirement under its licence to ensure that its charges are cost based, and like other originating operators, is free to set its own retention within Oftel's numbering parameters.

4.8 BT also argues that termination of calls to BT's freephone services is a BT standard service and is included in BT's list of standard services. BT argues that contractually the associated charge is a BT charge and should be set by BT, as negative POLO.

4.9 BT argues that calls to Freephone numbers present little scope for price manipulation. BT considers that this issue is not new, and that Oftel has previously considered representations from mobile operators who argued that the NTS regime, and the elements of reciprocity that went with it, did not allow them to recover their costs of call origination. BT considers that Oftel felt that it would be impractical for BT to make an allowance for higher costs of call origination on an operator by operator basis and to seek to reflect this in its contracts with service providers. Furthermore, BT states that Oftel concluded mobile operators could either charge for calls to freephone services (and use a recorded warning) or absorb the extra costs themselves. BT argues that these options are open to Telewest, and that BT (as a non-dominant terminating operator of NTS) should not be commercially penalised as a result of the costs of a less efficient operator.

4.10 BT argues that the purpose of the NTS regime is to encourage the development of competition at the terminating end. BT states that a consistency of approach is required, and considers that it would be unreasonable for its commercial freedom as a terminating operator to be constrained, in addition to the regulatory burden that it carries as an originating operator, where its right to set retail prices has already been removed. BT further considers that if Oftel directed that Telewest was able to receive increased payments from BT for calls to BT's freephone services, BT would have to renegotiate arrangements with service providers, by seeking more money from them. BT considers that this would undermine BT's position in the call termination market.

4.11 BT argues that if Telewest was able to increase the reverse POLO for Freephone calls other originating operators would follow suit, which would be difficult for BT to administer (due to the range of potentially different payments to originating operators, and the variety of commercial deals that BT would have depending on where a call was originated).

Telewest's letter of 18 April 2002

4.12 In relation to BT's argument that Telewest is able to set its own retention within Oftel's numbering parameters, Telewest considers that the current determination request concerns how Telewest can do this in practice, bearing in mind the charge is classed as a negative POLO charge within BT's carrier price list.

4.13 Telewest states that it currently has no intention of charging customers for making Freephone calls. Telewest considers that the current determination is fundamentally different from the mobile freephone origination issue that Oftel has previously considered, as Telewest has sought to recover the legitimate costs of

the same network elements for which BT charges, as opposed to introducing charges reflecting any costs which BT does not recover.

4.14 In response to BT's argument that there might be practical issues if the principle of Telewest recovering reasonable costs is accepted, Telewest states that dealing with such difficulties is part of day to day commercial reality. Telewest considers that such difficulties do not invalidate the basic principle that it is seeking a determination on.

4.15 Telewest states that it is merely trying to level the playing field in relation to the origination of freephone calls. Telewest states that BT pays a single tandem charge for freephone calls originating on BT's network, and that Telewest pays a higher amount overall for freephone calls terminating on its network and originating on BT's network. Telewest therefore states that it is misleading for BT to allege that Telewest's proposal would "commercially penalise" BT "as a result of the costs of a less efficient operator".

4.16 Telewest states that the rates proposed in Telewest's OCCN were derived from the same methodology used to set MSO call termination rates. Telewest states that within this approach is an assumption of equal efficiency.

Chapter 5

The Director's decision and reasons

5.1 The Director has carefully considered the arguments that have been submitted by the parties, as set out in Chapter 4.

5.2 Telewest has submitted an issue of principle for the Director to consider. The principle in question is whether Telewest can set a price to BT which covers the reasonable costs that Telewest incurs when originating a freephone call on its network. In issuing this determination, the Director will take into account the criteria set out in Regulation 6(8) of the Regulations, inter alia, the relative market positions of the parties to the dispute, the desirability of obtaining equal access arrangements and the interests of users. The Director will also take into account his duties to encourage and secure adequate interconnection in the interests of all users in a way that provides maximum economic efficiency and gives maximum benefit to end users. The Director considers that if neither party to the dispute has market power, they will be best placed to make their own commercial decisions which will drive down costs and deliver maximum benefits to end users.

Technical analysis

5.3 As set out in paragraph 4.3, Telewest currently receives BT's single tandem charge, uplifted by relevant retail costs, for originating NTS traffic that terminates on BT's network. Telewest has submitted this determination request because it considers that BT's single tandem charge is inappropriate, due to the increased costs that Telewest faces in originating calls on its network. At this stage it is necessary to elaborate on the technical differences between Telewest's network and BT's network.

5.4 The charging structure for call origination by BT is based primarily on the number of switching stages. All single tandem calls generate the same charge, irrespective of the distance travelled. Transmission costs are only explicitly considered when the different tiers of double tandem charges are considered. Although BT's costs are based on the number of switching stages, the costs which these charges are intended to cover relate primarily to transmission, not switching.

5.5 Network architecture and subscriber density will differ between operators. An operator serving a smaller subscriber density has fewer switches, and longer transmission links between them. Therefore it is plausible that a single tandem call originating on one operator's network will be directly comparable in terms of transmission costs with a double tandem call originating on BT's network.

5.6 As set out in paragraph 3.9, the Director requested further information from Telewest on the routing analysis that Telewest had undertaken in order to identify that 18% of freephone calls involved a tandem leg within the Telewest network before being delivered to BT. Without fettering the discretion of the Director

regarding the case before him, it appears that the figure of 18% that Telewest has arrived at is justified.

Market analysis

5.7 In considering the issue that has been referred, the Director needs to assess whether there is a valid reason why Telewest should not be able to recover the legitimate costs that are associated with originating a freephone call on its network. The Director will now consider the relative market positions of the parties to this dispute.

5.8 It is first necessary to consider the market in which Telewest is operating. Telewest is originating freephone calls, and if the origination of freephone calls was analogous to call termination for a geographic call, Telewest would hold a position of market power. However, if call origination for freephone calls has the same characteristics as call origination generally, Telewest would be operating in the wider call origination market, and Telewest would not hold a position of market power. These two potential markets will now be considered further.

5.9 For freephone calls, the call recipient pays the charge, including the charge for the call origination service provided by the originating network. It could be argued that this scenario is analogous to the situation for call termination of a geographic call. In geographic call termination, the terminating operator has market power because the caller would have no choice but to pay whatever is charged by the terminating operator.

5.10 If this argument was accepted, the rationale for regulatory intervention in call termination of a geographic call might also apply to the origination of a freephone call, as an excessive charge set by originating operator (in this case Telewest) would have to be paid by the terminating operator (in this case BT).

5.11 However, the Director does not consider that call origination for a freephone call is equivalent to call termination for a geographic call. For a normal call, the caller is wishing to contact a particular person, and the caller has no choice about which network to use. The caller is obliged to use the network chosen by the call recipient, or not make the call at all. The caller would not have sufficient knowledge to identify the network that the recipient was on, and the charges for calling that network.

5.12 In the case of freephone calls, recipients are seeking to receive calls from a number of callers unknown to them. If an originating operator (which does not hold a position of market power in call origination) attempts to propose an unreasonable charge, recipients could identify the originating network that is charging excessively, and choose not to receive calls from that network. This would prevent customers on that originating network from making freephone calls, which would, in turn, induce that network to reduce the charges to the competitive

level. As a result, the externality that is present in call termination is not considered to be present in the case of freephone call origination.

5.13 Therefore the Director considers that call origination for a freephone call is not sufficiently similar to call termination for a geographic call. Instead, freephone call origination has the same characteristics as call origination for a geographic call. Given that this is the case, Telewest's market share in wholesale call origination (the relevant economic market) can be proxied by its market share by volume of calls, which gives a figure of 6.5%¹ for 2001/02 Q3. Telewest is not dominant in this market. BT has a market share of 24.8 %² in the NTS call termination market for 2001/2 Q3, so it is unlikely to be dominant in this market. In addition, *Oftel's Statement on Effective Competition in the NTS market* (see www.oftel.gov.uk/publications/numbering/2002/nts0302.htm) confirmed that the market for retail voice NTS is effectively competitive.

5.14 Given this market analysis, the Director considers that Telewest should be able to propose its own charge for the cost of originating freephone calls, as the conditions of competition are such that neither party is in a position to enforce an unreasonable charge. Therefore appropriate charges will be achieved via commercial negotiation between originating operators (other than BT) and terminating operators.

5.15 However, it should be noted that this principle only applies to the origination of freephone traffic. If in the future a dispute was referred to the Director regarding the ability of an originating operator (other than BT) to propose its own charge for the origination of non-freephone NTS traffic, the Director's discretion to take a different view in light of circumstances could not be fettered. In resolving an interconnection dispute the Director must take into account the criteria set out in Regulation 6(8) of the Regulations, inter alia, the interests of users, and the desirability of stimulating innovative market offerings and of providing users with a wide range of telecommunications services.

The resolution of disputes between non-dominant operators

5.16 The analysis set out in paragraphs 5.7-5.15 has shown that neither party to this dispute holds a position of dominance in the relevant economic market. In this case, and as demonstrated above, the parties have a commercial incentive to reach agreement on the matter in dispute. BT has, however, rejected Telewest's proposed charge on the basis that the proposal does not accord with the NTS regime. As a result, the parties are in dispute, and Telewest has referred the matter to the Director for resolution. The Director is therefore required to issue a determination as to whether Telewest can propose its own charge under the NTS regime.

¹ Source: Oftel market information.

² Source: Oftel market information.

5.17 On 24 April 2002, a number of new EC Directives came into force, and these must be implemented into UK law by 25 July 2002. The way the Director resolves disputes between operators will be amended, in line with the provisions of Article 20 of Directive 2000/21/EC on a common regulatory framework for electronic communications networks and services (Framework Directive). Article 20 of the Framework Directive sets out the obligations of Member States in relation to dispute resolution between undertakings. The Director is currently considering how disputes and casework will be handled following the implementation of the new EC Directives.

5.18 It is the Director's intention to ensure that disputes between non-dominant operators can be resolved as efficiently as possible. For example, it may be that there are a number of methods of dispute resolution which could be available to the Director, including, for example, mediation. The Director is seeking to ensure that if there is a commercial incentive for operators to reach agreement on a particular issue, the dispute resolution procedure that is adopted should reflect this. The Director will be consulting on this issue later in the year.

The Director's response to BT's arguments

5.19 BT's arguments provided in support of its rejection of Telewest's OCCN of 23 November 2001 will now be considered. The Director will consider these arguments in order to ascertain whether there are any legitimate reasons why the Director's previous position, as outlined in the 1999 NTS statement, should not continue to apply. As previously stated, this position is that originating operators other than BT are free to propose their own originating charges, and negotiate the payments required for access to their services with terminating operators.

5.20 BT's arguments can be broken down into four broad categories. First, BT has argued that the charge for originating a freephone call should be set contractually between the parties. Second, BT has argued that previous Oftel precedent indicates that the Director should not grant Telewest's determination request. Third, BT has argued that Telewest's request would be difficult to implement. Fourth, BT has argued that Telewest's request, if granted, would undermine BT's position in the call termination market.

BT's contractual arrangements

5.21 BT has stated that termination of Freephone calls is a standard service, and should therefore be set by BT as negative POLO. In this respect BT is saying that because its freephone service is a standard service (and therefore Oftel sets the charge under the Network Charge Control) Telewest cannot challenge the charge.

5.22 Oftel does not consider that this argument is valid. The OCCN process is a contractual matter and an OLO can issue an OCCN in order to seek a change. This is what Telewest has sought to do in the present case.

Consistency of Oftel's approach

5.23 BT raises two issues with regard to the historic approach that it considers has been taken by Oftel. First, BT argues that Oftel has always sought to set in place arrangements which increase the number of services available at the terminating end, and that this approach would indicate that Telewest's determination request should not be granted. Second, BT argues that Oftel's previous conclusion on whether mobile operators should be able to recover their origination costs indicates that Telewest's request should not be granted. These two arguments will now be considered.

Emphasis on availability of services at the terminating end

5.24 The new NTS regime allows terminating operators the flexibility to set the retail prices at which their services are made available to customers. Terminating operators set their own terminating charge. Once this charge is added to the BT origination charge, which is set by Oftel, the sum of these two charges is the price at which terminating operators retail their services to consumers. However, as previously stated, the new NTS regime allows originating operators other than BT to set their own origination charges. The Director considers that this approach gives service providers, in conjunction with terminating operators, the opportunity to decide how to pitch their prices in the retail market and compete aggressively on both price and service content.

5.25 As set out in paragraphs 5.7-5.15 the Director considers that the conditions of competition between operators originating Freephone calls (other than BT) and operators terminating freephone calls are such that the parties have a commercial incentive to reach agreement on the relevant payments between them. Neither the originating operator nor the terminating operator will hold a position of market power. If a freephone service provider considers that a charge set by a terminating operator is excessive, that service provider is free to seek different arrangements with other terminating operators.

5.26 Without fettering his discretion to take a different view in the light of circumstances, the Director also currently considers that these commercial arrangements should apply to freephone calls that terminate on the networks of all terminating operators, not just BT. Terminating operators will have an incentive to compete for this Freephone business, and will be best placed to make a commercial decision about the prices that they can charge. As a result, it does not appear that Telewest's request is likely to have a material adverse impact on the availability of Freephone services at the retail level.

Mobile operators & freephone call origination

5.27 BT has stated that Oftel has previously considered this issue, in relation to representations from mobile operators that the NTS regime did not allow them to

cover their costs of call origination. BT considers that, as is the case with mobile operators, Telewest could cover its costs of originating freephone calls by either charging customers for dialling freephone numbers, or accepting losses on such calls.

5.28 Originating operators are able to adopt pricing strategies for Freephone calls in accordance with the provisions of the Numbering Conventions that are issued by the Director. The most recent *Numbering Conventions for the United Kingdom*, (see www.oftel.gov.uk/ind_info/numbering/nconv1101.htm) issued on 1 March 2002, state that freephone calls are to be free to the caller, except on certain networks where charges shall be notified to callers at the start of the call. In principle, the Director considers that freephone calls should be free to the caller.

5.29 BT also states that elements of reciprocity within the NTS regime did not enable mobile operators to recover their costs of call origination. As set out in paragraph 2.13, Oftel supports the principle of reciprocity in the context of the termination of geographic calls, due to the network externality that exists. However this externality does not exist in the current issue under consideration. Therefore the arguments that warrant reciprocity in the termination of geographic calls do not apply to the origination of freephone calls.

Ease of implementation

5.30 BT argues that the implementation of Telewest's request would raise two particularly difficult administrative issues. First, BT states that the implementation of Telewest's request would result in BT having to administer a number of different payments to originating operators. Second, BT states that the implementation of Telewest's request would mean that it would need to have a variety of different agreements with service providers, which would differ according to where a particular call originated.

5.31 The Director is not persuaded by BT's argument regarding the difficulty of making different payments to originating operators. BT has arrangements in place in other areas where different charges are made for different operators. For example under the Network Charge Differential regime, the call termination rate depends on the point of connection count of the terminating operator. BT is able to exact different amounts from terminating operators to whom it originates Freephone calls, as BT invoices each terminating operator according to its connectivity with BT. Therefore it does not appear to Oftel that there are convincing reasons why BT as a terminating operator cannot administer different payments to originating operators.

5.32 As set out in paragraph 1.7, the Director also considers that originating operators other than BT should be able to set charges to all terminating operators (ie not just BT) which cover the costs of originating freephone calls. In the absence of direct interconnection between originating operators and terminating operators, freephone traffic will need to be transited between each operator's network. The

Director is aware of technical issues associated with billing for transit calls, but believes that the appropriate mechanisms are being discussed that will enable the costs of originating freephone calls to be recovered.

5.33 The Director has also considered BT's argument that the implementation of Telewest's request would require BT to have a variety of different agreements with service providers, which would differ according to where the call was originated. Oftel considers that as it possible to identify where a call is originated, implementing new arrangements with service providers should not be an unduly onerous task for BT.

The potential for BT's position in the call termination market to be undermined

5.34 BT has contrasted its position in the originating market with that of Telewest's, and has argued that whilst BT's retention is regulated (due to Oftel determining it to be dominant in this market), Telewest has no such restriction on its ability to set charges. BT is concerned that Telewest might seek to over-recover costs incurred when originating freephone calls on its network. BT states that Telewest's request, if granted, could enable Telewest to set unreasonably high charges to BT and therefore undermine BT's position in the call termination market.

5.35 The Director has carefully considered whether granting Telewest's request would undermine BT's position in the call termination market. As set out in Paragraphs 5.7-5.15, neither Telewest or BT possesses market power, and so they have a commercial incentive to reach agreement over the pricing arrangements that govern the origination of freephone calls by Telewest which terminate on BT's network. Therefore the Director is resolving this dispute by allowing Telewest to propose its own charge, as a reasonable price will be achieved via negotiation between the parties to the dispute.

5.36 However, the Director has also considered the impact that the granting of Telewest's request might have on competition between BT and other terminating operators. Although outside the scope of this draft direction, the Director currently considers that for reasons of equity and proportionality, Telewest and other non-dominant originating operators should be able to set in place their own arrangements for originating freephone calls that terminate on other networks, not just BT's. This, of course, is the Director's current view, and his discretion to take a different view in the light of circumstances cannot be fettered.

The proposed decision

5.37 Having considered the arguments for and against Telewest's request, the Director is minded to direct that:

- (i) Telewest may propose its own price for the charge of originating a Freephone call that originates on Telewest's network and terminates on BT's network.

Implementation

5.38 Telewest has asked the Director to issue a determination on an issue of principle. In its initial submission to the Director, Telewest stated that the approach that it has taken in attempting to implement the requested principle is the same as the approach adopted by multi-switch operators under the PSTN 'reciprocity' regime for call termination.

5.39 The Director does not propose to mandate a particular approach that the parties must follow in order that Telewest's request is adopted. The parties should negotiate in order to ensure that a symmetrical competitive situation in call origination is achieved.

Chapter 6

Consultation and timetable for responses

6.1 The Director General's draft decision is being made available to interested parties, together with the Director General's reasons, so that they may have a reasonable opportunity to make representations.

6.2 Please e-mail or send comments in writing to:

Robert MacDougall
OfTel
50 Ludgate Hill
London
EC4M 7JJ

tel: (020) 7634 8726
fax: (020) 7634 8738
e-mail: robert.macdougall@oftel.gov.uk

6.3 Comments on this consultation must be sent to OfTel by 24 July 2002. OfTel does not intend on this occasion to hold any comments-on-comments phase during which observations may be made on the representations made by others. Nevertheless, in the interests of transparency, all non-confidential representations will be published.

6.4 Confidential responses should not be sent via e-mail. Written comments will be made publicly available in OfTel's Research and Intelligence Unit, except where a respondent indicates that a response, or part of it, is confidential. Respondents are therefore asked to separate any confidential material into a clearly marked annex. In the interests of transparency, respondents are asked to avoid confidential markings wherever possible.

6.5 The final Direction will be made as soon as possible after the end of the above mentioned consultation period.

Annex A – Schedule of operators in the Telewest Group of companies

Operator	Franchise	Date of Agreement
<i>Telewest Communications plc</i>	National Licence – No Franchises	15 Jan 1998
<i>Various Operators Telewest</i>	Telewest Communications (Central Lancashire) Ltd	26 Sep 1996
	Telewest Communications (Cotswolds) Ltd	26 July 1996
	Telewest Communications (Cumbernauld) Ltd	22 Aug 1996
	Telewest Communications (Dumbarton) Ltd	22 Aug 1996
	Telewest Communications (Dundee & Perth) Ltd (Dundee Franchise)	22 Aug 1996
	Telewest Communications (Dundee & Perth) Ltd (Perth Franchise)	22 Aug 1996
	Telewest Communications (Falkirk) Ltd	22 Aug 1996
	Telewest Communications (Glenrothes) Ltd	22 Aug 1996
	Telewest Communications (Liverpool) Ltd (North Liverpool & Sefton Franchise)	26 Sep 1996
	Telewest Communications (Liverpool) Ltd (Merseyside Franchise)	26 Sep 1996
	Telewest Communications (London South) Ltd (Kingston & Richmond Franchise)	26 Sep 1996
	Telewest Communications (London South) Ltd (Merton & Sutton Franchise)	26 Sep 1996
	Telewest Communications (London South) Ltd (Croydon Franchise)	26 Sep 1996
	Telewest Communications (Midlands) Ltd	26 Sep 1996
	Telewest Communications (Motherwell) Ltd	22 Aug 1996
	Telewest Communications (North East) Ltd (Newcastle & Gateshead Franchise)	1 Sep 1996
	Telewest Communications (St Helens & Knowsley) Ltd	26 Sep 1996
	Telewest Communications (Scotland) Ltd (Edinburgh Franchise)	22 Aug 1996

	Telewest Communications (South East) Ltd	26 Sep 1996
	Telewest Communications (South Thames Estuary) Ltd	26 Sep 1996
	Telewest Communications (South West) Ltd	26 July 1996
	Telewest Communications (Telford) Ltd	26 Sep 1996
	Telewest Communications (Wigan) Ltd	26 Sep 1996
<i>Various Operators General Cable (TCC)</i>	Windsor Television Limited (Windsor)	11 Sep 1996
	Windsor Television Limited (Iver)	11 Sep 1996
	Middlesex Cable Limited	11 Sep 1996
<i>Various Operators General Cable (YCC)</i>	Barnsley Cable Communications Ltd	11 Sep 1996
	Doncaster Cable Communications Ltd	11 Sep 1996
	Halifax Cable Communications Ltd	11 Sep 1996
	Sheffield Cable Communications Ltd	11 Sep 1996
	Yorkshire Cable Communications Ltd	11 Sep 1996
	Wakefield Cable Communications Ltd	11 Sep 1996
<i>Birmingham Cable Limited</i>	No individual Franchise areas - contract applies to whole Birmingham Cable Franchise	24 Oct 1996
<i>Various Operators (Cable London)</i>	Cable Camden Limited	30 Sep 1996
	Cable Enfield Limited	30 Sep 1996
	Cable Hackney & Islington Limited	30 Sep 1996
	Cable Haringey Limited	30 Sep 1996
