



Openreach response to Ofcom's Consultation on its proposal to issue a direction specifying the fair and reasonable charge for MPF Rental at Service Maintenance Level 1

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**NON-CONFIDENTIAL VERSION**

Comments on this response should be sent to:

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## 1. INTRODUCTION

1.1. This submission is provided on behalf of British Telecommunications plc ("**BT**") by Openreach, a functionally separate line of business within BT,<sup>1</sup> in response to Ofcom's Consultation on its proposal to issue a direction specifying the fair and reasonable ("**F&R**") charge for Metallic Path Facilities ("**MPF**") Rental at Service Maintenance Level 1 ("**SML1**") (the "**Proposal**") of 31 March 2017 (the "**Consultation**"). Ofcom asks one consultation question:

*"Do you agree with our proposal to impose a direction specifying the fair and reasonable charge that BT may apply for MPF (SML1) rental? Please provide your reasons and any evidence in support of your views."*<sup>2</sup>

1.2. This submission is structured as follows:

- (a) Section 2 is an executive summary;
- (b) Section 3 sets out the factual and regulatory background to the Consultation;
- (c) Section 4 sets out the legal framework applicable to the Proposal to direct a F&R price;
- (d) Section 5 explains why BT's current charges for MPF SML1 are not excessive and its Commitment is F&R;
- (e) Section 6 explains why there is no lawful rationale for the Proposal;
- (f) Section 7 explains why the Proposal is more generally, from regulatory and policy perspectives, inappropriate; and
- (g) Section 8 sets out, without prejudice the submissions made in the above sections, in the event Ofcom implements the Proposal, a number of obvious gaps that must be addressed.

## 2. EXECUTIVE SUMMARY

***Openreach looks forward to proactively and constructively engaging with Ofcom***

- 2.1. Since Spring last year, at Ofcom's behest, Openreach (and BT) has engaged proactively and constructively with Ofcom in order to address Ofcom's concerns about pricing transparency and certainty for a range of products during the regulatory "gap" or lacuna for the period between 31 March 2017 and the introduction of the next price control (now planned for 1 April 2018) (the "**Lacuna Period**"). That culminated in Openreach (and BT) voluntarily committing to hold prices for a range of products, including for MPF rentals, during the Lacuna Period (the "**Commitment**"). That Commitment was made in good faith.
- 2.2. Openreach is of the firm view that the Consultation and the Proposal to direct a F&R charge of £84.38 for MPF SML1 is wrong, both in law and in policy. In addition, the Proposal gives rise to a range of unintended negative consequences which Ofcom has failed to take into account.

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<sup>1</sup> As part of BT's implementation of its formal notification dated 10 March 2017 under section 89C of the Communications Act (the "**Act**"), and subject to the conditions for implementation being met, the Openreach business will be operated by Openreach Limited, which was incorporated as a separate legal entity on 24 March 2017.

<sup>2</sup> Consultation, para 1.33.

Openreach accordingly urges Ofcom to reconsider its Proposal and re-engage directly with Openreach in order to reach a solution that both addresses Ofcom's concerns and does not give rise to the extensive legal and policy concerns and unintended negative consequences that Openreach has set out in this submission.

- 2.3. Nonetheless, Openreach is keen to continue constructive cooperation with Ofcom and would welcome the opportunity to meet to discuss how we could resolve any outstanding concerns that Ofcom has. Indeed, it would be preferable to resolve any outstanding concerns through dialogue and cooperation without the need for intrusive and unjustified *ex ante* regulation.

***The Proposal is wrong in law and policy***

- 2.4. Openreach has a number of serious concerns about Ofcom's Proposal, including:

- (a) the Proposal is unnecessary as BT's current charges for MPF SML1 are not excessive and its price commitment is F&R;
- (b) there is no lawful rationale for the Proposal, indeed Ofcom is acting contrary to its legal obligations, especially when the Proposal is compared to the Commitment; and
- (c) more generally, from regulatory and policy perspectives, the Proposal is inappropriate.

***BT's current charges for MPF SML1 are not excessive and the Commitment is F&R and provides the certainty Ofcom seeks***

- 2.5. In the Proposal, Ofcom has not evidenced any concerns about Openreach's current pricing and has not adduced any evidence to discharge its burden of proof that the MPF SML1 charge exceeds a lawful or fair level or goes beyond the legitimate bounds of a reasonable range.
- 2.6. Rather, Ofcom undertakes a very cursory analysis of what a F&R price entails without proper regard to relevant legal precedent and regulatory decisional practice on F&R. Indeed, Ofcom's approach is in conflict with its own previous decision making: it is incompatible with Ofcom's previous pronouncements on F&R (for example, that it provides for pricing flexibility and there being no single F&R price) and it is inappropriate for Ofcom retroactively to apply a forward looking charge control to a previous period in which only a F&R obligation applies.<sup>3</sup> Ofcom also fails to take into account the distinctions between a charge control and a F&R obligation, the latter recognised in law and policy as being a less intrusive, more flexible form of price regulation.
- 2.7. Further, nothing in the wider Wholesale Local Access Market Review Consultation published on 31 March 2017 (the "**WLA Consultation**") demonstrates that the current price for MPF SML1 of £85.29 is not F&R. Indeed, the WLA Consultation supports our view that the current price is F&R. Our current price is within the range that Ofcom is consulting on as part of its WLA Consultation (even where extrapolated back to the 2017/18 time period consistent with Ofcom's approach in formulating its Proposal). We have also already identified issues with the methodology adopted in the WLA Consultation suggesting that a higher base case price would be more appropriate.<sup>4</sup>

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<sup>3</sup> Access Directive, Recital 20; MPF Dispute, paras 4.31 and 4.43; Vodafone Limited, Telefónica O2 (UK) Limited, T-Mobile (UK) Limited and Orange Personal Communications Services Limited v. BT plc and Ofcom [2010] EWCA Civ 391.

<sup>4</sup> See paragraphs 5.15 to 5.16 of the submission below.

- 2.8. More generally, we find it odd for Ofcom to suggest that our current price is overnight not F&R given that it is derived from a charge control price (a stricter form of price regulation set by Ofcom) that applied for the period up to 31 March 2017.
- 2.9. Given the lack of evidence that the current MPF SML1 price is not F&R, the Proposal is clearly unnecessary and disproportionate. This is particularly so given that there are other more appropriate and less restrictive regulatory mechanisms for ensuring that Openreach complies with the F&R pricing obligation and, in particular, the Commitment already given by Openreach.

No lawful rationale for the Proposal

- 2.10. Ofcom's Proposal to direct a F&R price for MPF SML1 has no lawful rationale and, as such, falls outside the scope of Ofcom's lawful powers under the Act and the EU Common Regulatory Framework (the "CRF").
- 2.11. Ofcom proposes to impose an obligation on BT to adjust its prices in accordance with its directions regarding what it considers to be the correct price for MPF SML1. What is more, the Proposal is tantamount to setting a price control before the appropriate market analysis and consultation have been completed. The Proposal is a significant market power ("SMP") condition pursuant to section 87(9) of the Act, which cannot be set without observing the conditions in section 88 of the Act. Ofcom does not appear to have followed those steps or provided any reasoning as to why the imposition of the Proposal is necessary or appropriate.
- 2.12. The Act provides that such serious forms of regulatory intervention are subject to a prior market analysis and supported by reasoned justification on the basis that, absent the intervention, there is a risk of adverse effects from price distortion.<sup>5</sup> That entails an analysis of the potential effects of BT's pricing by reference to a realistic counterfactual – namely the pricing situation that would persist without the direction being in place. Ofcom has not undertaken this exercise.
- 2.13. Rather, Ofcom justifies intervention on the (unsubstantiated) grounds that it is necessary to ensure certainty, transparency and the charge for MPF SML1 is F&R. This is not correct. When the Proposal is assessed against the appropriate counterfactual (i.e. the current situation with the Commitment in place), it is clear that the current price is not unfair and that it does not distort prices. Therefore, *ex ante* intervention is not justified. Further, the Proposal does not provide any greater certainty or transparency than the Commitment. The Commitment was made well in advance of the Lacuna Period, provided certainty and transparency regarding pricing going forward and, for the reasons set out in this submission, is F&R. To the extent that there remains any uncertainty (which is not accepted), BT confirms that the Commitment includes a guarantee that it will maintain the price of £85.29 as the rental charge for MPF SML1 during the Lacuna Period. BT also confirms that it is willing to extend the Commitment until 1 April 2018 to take into account the fact that the new charge control is unlikely to be in place by 1 January 2018 (i.e. when the current Commitment expires).
- 2.14. For these reasons, the Proposal is not necessary, proportionate or targeted regulation. Ofcom has clearly failed to take account of its obligation to only impose burdens which are necessary as required by the Act.<sup>6</sup>

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<sup>5</sup> Act, section 88.

<sup>6</sup> Act, section 6.

*The Proposal is more generally, from regulatory and policy perspectives, inappropriate*

- 2.15. More generally, the Proposal is not consistent with best regulatory practice and is therefore inappropriate.
- 2.16. Firstly, Ofcom inappropriately conflates the purpose and implementation of two different regulatory conditions: F&R and charge control. It does this by proposing to direct the maximum level of a F&R charge which, on its face looks, and takes effect, like a charge control. This is particularly surprising given Ofcom has previously been at pains to separate these two regulatory conditions.<sup>7</sup>
- 2.17. Secondly, Ofcom is attempting to impose a de facto charge control for the Lacuna Period without undertaking the necessary market analysis, contrary to its legal obligations (as per section 86 of the Act) and appropriate regulatory practice.
- 2.18. Thirdly, Ofcom is effectively proposing the retroactive implementation of its projected charge control in the WLA Consultation which is still open to consultation and not expected to apply until 1 April 2018. This is a breach of the principle of non-retroactivity<sup>8</sup> and presupposes the outcome of an ongoing consultation. This raises serious legal questions about Ofcom's compliance with procedural requirements, due process and its wider regulatory obligations under the Act and the CRF.

***The Proposal gives rise to a number of unintended negative consequences***

- 2.19. By fundamentally changing its approach to assessing F&R, Ofcom is introducing significant uncertainty as to how a F&R pricing obligation should be applied. This leads to greater internal compliance costs, broader uncertainty and potentially more disputes. More generally, however, regulatory uncertainty and unnecessary regulatory intervention also have a chilling effect on investment.
- 2.20. Furthermore, Ofcom's proposal undermines the practical and legal value of Openreach giving voluntary commitments to Ofcom. BT provided the Commitment, on Ofcom's initiative, in August 2016 after a relatively long period of liaison between Ofcom and Openreach. Going forward, it is unclear whether regulated companies such as Openreach would have the same incentives to work collaboratively with Ofcom to minimise potential regulatory uncertainty and resolve concerns in future.
- 2.21. In the light of these concerns, BT strongly invites Ofcom to look afresh at its Proposal and to re-consider its merits, both as a short-term and long-term regulatory solution.

### **3. FACTUAL AND REGULATORY BACKGROUND**

- 3.1. In 2015, at the request of Local Loop Unbundling ("LLU") operators, Openreach introduced a lower cost variant of its MPF rental service in addition to the service it already offered. Whereas the original service (known as MPF Service Management Level 2 ("SML2")) had a next day commitment to fix faults, the new service (MPF SML1) had a next day + 1 commitment to fix but charged a lower price to reflect the lower level of service.

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<sup>7</sup> MPF Dispute, paras 4.28 to 4.31.

<sup>8</sup> MFP Dispute, paras 4.43; Vodafone Limited, Telefónica O2 (UK) Limited, T-Mobile (UK) Limited and Orange Personal Communications Services Limited v. BT plc and Ofcom [2010] EWCA Civ 391.

- 3.2. The prices for MPF SML2, Shared Metallic Path Facilities (“SMPF”) and Wholesale Line Rental (“WLR”) were subject to price regulation, following the 2014 Fixed Access Market Review (“2014 FAMR”) in the form of a SMP charge control. MPF services are also subject, following the 2014 FAMR, to an ongoing condition to provide MPF rental on F&R terms (the “F&R obligation”).<sup>9</sup> The price of MPF SML1 was not regulated by a charge control since it was introduced after the publication of the relevant FAMR statement(s) but they remain subject to the F&R obligation as part of BT's network access obligations. Instead, BT set the price of the MPF SML1 service at a discount from Ofcom's regulated price cap for MPF SML2. The current rental price for MPF SML1 is the MPF SML2 price (£87.65) discounted by £2.19 per line, that is £85.29.
- 3.3. Between March 2016 and March 2017, the key LLU operators (Sky and TalkTalk (“TT”)) decided to migrate most of their MPF SML2 lines to the lower service level MPF SML1 in order to benefit from the discounted price.
- 3.4. The charge control for MPF SML2 services imposed under the 2014 FAMR had a fixed duration of 3 years, which was due to expire on 31 March 2017. In as early as Spring 2016 Ofcom realised the next WLA market review would be subject to a delay. That meant that a new charge control for MPF SML2 would not be in place prior to the expiry of the then existing charge control. That meant also there would be a regulatory “gap” or lacuna for the period between 31 March 2017 and the introduction of the next price control (now planned for 1 April 2018) (that is, the Lacuna Period). Ofcom approached Openreach to discuss what voluntarily arrangement Openreach would be willing to make to cover the Lacuna Period.
- 3.5. Following lengthy discussions, Openreach offered by letter on 2 August 2016 to make a voluntary commitment to cap rental prices for MPF, SMPF and WLR services at the current (2016/17) rental charge.<sup>10</sup> It did so at the behest of Ofcom and in the interests of providing pricing certainty during the Lacuna Period, bearing in mind its ongoing obligations to provide MPF rental on F&R terms during the Lacuna Period.<sup>11</sup>
- 3.6. As part of the voluntary commitments welcomed by Ofcom, Openreach committed to hold MPF SML2 prices at the regulated price of £87.65 during the Lacuna Period. That meant, as recognised by Ofcom, it also “effectively committed to charge £85.29 for MPF (SML1)”<sup>12</sup> during the Lacuna Period (that is, the Commitment). That discounted rate being derived directly from the regulated price cap for MPF SML2.
- 3.7. On 31 March 2017, Ofcom published the WLA Consultation, in which it proposed to impose a charge control for MPF SML1 rather than for MPF SML2 (as was previously the case). The WLA Consultation includes (amongst other matters) detailed cost considerations which Ofcom

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<sup>9</sup> FAMR Condition 1.2 provides that “[e]xcept where condition 1.3 applies, the provision of network access...must...be on...fair and reasonable terms, conditions and charges”. FAMR Condition 1.3 provides that, “[w]here any of conditions 6 or 7 apply (with the exception of condition 7A.9)...the provision of network access must be on fair and reasonable terms and conditions (excluding charges).”

<sup>10</sup> The voluntary commitment was made when it was expected that Ofcom's WLA Market Review would be delayed by 9 months and therefore applied to 31 December 2017. As a result of further delays, the Lacuna Period is now expected to be longer.

<sup>11</sup> The net effect FAMR Conditions 1.2 and 1.3 is that, in relation to MPF, the provision of the charge control as set out in FAMR Condition 7 and provided for in FAMR Condition 1.3 only has effect during the defined Relevant Years (i.e. up to 31 March 2017). From 1 April 2017, FAMR Condition 1.3 does not apply but FAMR Condition 1.2 continues to take effect. [http://stakeholders.ofcom.org.uk/binaries/telecoms/ga/fixed-access-market-reviews-2014/statement-june-2014/Annex\\_29.pdf](http://stakeholders.ofcom.org.uk/binaries/telecoms/ga/fixed-access-market-reviews-2014/statement-june-2014/Annex_29.pdf).

<sup>12</sup> Consultation, para 1.15.

uses to generate a range and base case for the proposed price cap for MPF SML1 and a glidepath for the next review period. The response date is 9 June 2017 and BT is in the process of preparing its detailed submissions on all the issues raised, not least the range, base case and glidepath for MPF SML1. It is not expected that the WLA Market Review final statement will be confirmed, given extensive likely inputs from all interested stakeholders, before early 2018.

- 3.8. At the same time as issuing the wider WLA Consultation, notwithstanding Openreach's commitment to hold MPF SML1 prices at the discounted rate of £85.29 during the Lacuna Period, Ofcom also published a separate proposal to issue a direction to set the rental price for MPF SML1 at the lower charge of £84.38 during the Lacuna Period. The proposed price is extrapolated using a glidepath back from year 1 price proposed in the WLA Consultation (to apply from 1 April 2018). That year one price has been set using a glidepath by reference to an estimate of long run incremental cost plus ("LRIC+") at year 3 of the next charge control (2020/21).

#### 4. THE LEGAL FRAMEWORK

##### *Ofcom's statutory powers to set SMP conditions*

- 4.1. Ofcom has the power to set SMP conditions under section 45(2)(iv) of the Act, which implements the CRF. The Framework Directive and Access Directive from the CRF are the most pertinent in terms of Ofcom's regulatory duties and objectives, which are implemented by sections 3 and 4 of the Act.
- 4.2. The categories of SMP conditions which Ofcom is entitled to make are set out in section 87 of the Act. Insofar as is relevant, section 87 of the Act provides that:
- (a) under section 87(3), Ofcom may impose conditions requiring the dominant provider to give such entitlements as Ofcom may direct in relation to the provision of network access;
  - (b) under section 87(5), conditions imposed under section 83(3) may include provision for securing fairness and reasonableness in the way in which the requests for network access are made and responded to; and
  - (c) under section 87(9) of the Act, the SMP conditions authorised by section 87 "*also include (subject to section 88) conditions imposing on the dominant provider – (a) such price controls as OFCOM may direct ... and (d) obligations to adjust prices in accordance with such directions given by OFCOM as they may consider appropriate*".
- 4.3. Ofcom may only set or modify an SMP condition if it is objectively justifiable, not unduly discriminatory and proportionate to what the condition or modification is intended to achieve and, in relation to what it is intended to achieve, transparent.<sup>13</sup> Further, if the SMP condition involves imposing a price control or an obligation to adjust prices, Ofcom may only make this condition if:
- (a) It appears to Ofcom from the market analysis carried out for the purpose of setting that condition that "*there is a relevant risk of adverse effects arising from price distortion*".<sup>14</sup> There will be a relevant risk of adverse effects if the provider with SMP might fix and

<sup>13</sup> Act, section 47(2).

<sup>14</sup> Consultation, para 1.24.

maintain prices at an excessively high level, or impose a price squeeze so as to have adverse consequences of end users.

- (b) It also appears to Ofcom that the setting of the condition is appropriate for the purposes of efficiency, promoting sustainable competition, and conferring the greatest possible benefits on the end-users of public electronic communication services.<sup>15</sup>

- 4.4. These conditions reflect Article 8 of the Framework Directive, which requires Ofcom to apply objective, transparent, non-discriminatory and proportionate regulation, including by ensuring a consistent regulatory approach and only imposing *ex ante* regulatory obligations where there is no effective and sustainable competition.<sup>16</sup> They also reflect Article 13(1) of the Access Directive, which makes clear that a national regulatory authority may only impose obligations relating to cost recovery and price controls where a market analysis indicates a lack of effective competition meaning that the operator concern may sustain excessively high prices or apply a price squeeze to the detriment of end users.
- 4.5. A further condition relating to the modification of SMP conditions is that Ofcom may not modify a SMP service condition (which includes obligations under section 87 of the Act) unless it has carried out an analysis of the market under section 84 of the Act, or it is satisfied that there has not been material change in the market since the condition was set.<sup>17</sup>

#### ***SMP conditions in the FAMR 2014***

- 4.6. In the FAMR, so far as is relevant to the Proposal, Ofcom imposed the following SMP conditions on BT:
- (a) Under condition 1.2(b), Ofcom required the provision of network access by BT, save where conditions 6 or 7 applied, to be on:
- “(i) fair and reasonable terms, conditions and charges; and*
- (ii) such terms, conditions and charges as OFCOM may from time to time direct.”*
- (b) Under condition 7, Ofcom imposed a charge control on BT for the rental price of MPF (specifically MPF SML2) setting the maximum price for each of the years 2014/15, 2015/16 and 2016/17. As noted above, those charges expired on 31 March 2017.

#### ***F&R terms, conditions and charges***

- 4.7. The rationale for the F&R condition is to ensure competition downstream and to mitigate the risk of a margin squeeze and it follows that, as Ofcom has acknowledged, a range of charges may be F&R.<sup>18</sup> Ofcom has also acknowledged that the meaning of F&R may vary depending on the particular circumstances of the service to which it applies.<sup>19</sup>

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<sup>15</sup> Act, section 88.

<sup>16</sup> See also Act, section 3.

<sup>17</sup> Act, sections 86(2) to (4). As set out in paragraphs 7.10 to 7.12 of this submission below, Ofcom has not carried out the necessary analysis.

<sup>18</sup> MPF Dispute, para 4.23; MPF New Provide Dispute (No 2), paras 4.19 to 4.20.

<sup>19</sup> FAMR 2014, para 10.42.

4.8. Legal precedent and regulatory decisional practice make it clear that:

- (a) F&R is designed to give pricing flexibility.<sup>20</sup>
- (b) F&R does not imply that there is a single “correct” price.<sup>21</sup> Ofcom has previously stated that it cannot reliably assess the relative likelihood that a particular value in a range is more likely to be F&R than another.<sup>22</sup> Ofcom has further noted that the obligation around terms and conditions is to be “*fair and reasonable, not to be the “most” fair and reasonable terms possible*”.<sup>23</sup>
- (c) F&R allows for BT's costs to be taken into account and to allow for common cost recovery.<sup>24</sup>
- (d) There is no set cost standard for assessing compliance with a F&R pricing obligation.

4.9. For these reasons, an obligation to impose F&R charges may be distinguished from a charge control which sets a specific price. As Ofcom has noted, charge control and the obligation to provide access on F&R terms, conditions are charges “*are separate and designed to operate independently of each other*” and “*intended to provide ex ante regulation through different mechanisms*”.<sup>25</sup> Accordingly, Ofcom's does not consider that “*the SMP Condition relating to Network access, in the absence of a SMP Condition imposing a charge control, implies that there is only a single price which would satisfy the obligation.*”<sup>26</sup>

4.10. More detail on the meaning and application of F&R charges is provided in section 7 of this submission below.

## 5. BT'S CURRENT CHARGES FOR MPF SML1 ARE NOT EXCESSIVE AND ITS PRICE COMMITMENT IS F&R

### ***No evidence that the current price is excessive***

- 5.1. In the Proposal, Ofcom has not evidenced any concerns that Openreach's current pricing is other than F&R, which is the regulatory condition that applies during the Lacuna Period. Further, Ofcom has not adduced any evidence to discharge its burden of proof that the MPF SML1 charge exceeds a lawful or fair level or goes beyond the legitimate bounds of a reasonable range. Nothing in the wider WLA Consultation, in which Ofcom is consulting on the charge control price to apply for a future period, demonstrates that the current price of £85.29 is not F&R for the Lacuna Period.
- 5.2. Indeed, given that MPF SML1 charges have been set by reference to the regulated price cap that Ofcom set for MPF SML2 (applied until 31 March 2017) and are lower than that maximum regulated charge, it is hard to see how they could be said to be unfair or excessive.
- 5.3. Moreover, as part of the Commitment, BT has given an assurance that it will continue to apply the current prices for MPF (both SML2 and SML1) during the Lacuna Period. For the

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<sup>20</sup> Access Directive, Recital 20.

<sup>21</sup> MPF Dispute, para 4.31.

<sup>22</sup> MPF New Provide Dispute No. 1 (2013), para 4.22.

<sup>23</sup> MPF New Provide Dispute No. 1 (2013), para 4.23.

<sup>24</sup> FAMR 2014, para 10.83.

<sup>25</sup> MPF Dispute, para 4.31.

<sup>26</sup> MPF Dispute, para 4.31.

avoidance of all doubt, BT confirms that the Commitment includes a guarantee that it will maintain the price of £85.29 as the rental charge for MPF SML1 during that period. BT also confirms that it is willing to extend the Commitment until 1 April 2018 to take into account the fact that the new charge control is unlikely to be in place by 1 January 2018 (i.e. when the current Commitment expires).

- 5.4. Openreach has considered, in light of the WLA Consultation, whether the Commitment as regards the MPF SML1 price remains consistent with our obligation to provide network access on F&R charges in FAMR Condition 1.2(a). Openreach remains confident that, by reference to established F&R principles (as set out in paragraphs 4.8 of this submission above) and the WLA Consultation, the current MPF SML1 price of £85.29 is F&R.<sup>27</sup>

***Ofcom's framework for assessing whether intervention is necessary is wrong***

- 5.5. Ofcom has undertaken a very cursory analysis of what a F&R price entails, failing to address the general principles that have been established in its previous decisional practice to date. That regulatory inconsistency is starkest when Ofcom contradicts its previous stance that a F&R pricing obligation does not imply a single, best or correct F&R price but permits a reasonable range.<sup>28</sup> In addition, Ofcom has not taken into sufficient account the fact that there are existing regulatory mechanisms for both Ofcom and communications providers to ensure compliance with the F&R pricing obligation.

- 5.6. First, and in particular, Ofcom has set out an incorrect legal test for identifying a F&R charge. Ofcom states:

*"Unlike a formal charge control, which may set a specific charge following detailed modelling, identifying a fair and reasonable charge requires us to identify the best proxy from within a range of charges that may be fair and reasonable".<sup>29</sup>*

- 5.7. However, there is no authority for this being the appropriate legal test to apply when identifying a F&R charge. There is no legal basis for Ofcom being required to identify the "best" proxy or indeed any indication what the "best" proxy should be. Indeed, Ofcom's formulation of the legal test contradicts the principles that Ofcom itself has established as to how it should apply F&R, in particular that there is no single or best correct price and that F&R is intended to afford pricing flexibility.<sup>30</sup>

- 5.8. Indeed, Ofcom's assertion that the ongoing WLA Consultation data sets the best proxy for a F&R charge is inconsistent with previous Ofcom decisional practice. By way of example, Ofcom stated in its determination of a dispute between TT<sup>31</sup> and Openreach relating to the MPF rental charge in January 2012 ("**MPF Dispute**"):

*"We do not therefore agree with TTG that the data on which we consulted in the March and/or November 2011 Consultation suggests a single charge that would meet SMP Condition FAA1 (i.e. to provide network access on fair and reasonable terms, conditions and charges). We therefore also disagree that Openreach is obliged to amend its charges so as to ensure that its charges are aligned with those set out in the March / November 2011 Consultation.*

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<sup>27</sup> See paragraphs 5.12 to 5.17 of this submission below.

<sup>28</sup> MPF Dispute, para 4.31.

<sup>29</sup> Consultation, para 1.21.

<sup>30</sup> Access Directive, Recital 20; MPF Dispute, para 4.31.

<sup>31</sup> Referred to as TTG in Ofcom's determination.

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*As outlined in paragraphs 4.26 to 4.31 above, we do not consider that compliance with SMP Condition FAA1 (in the absence of a SMP Condition imposing a charge control), implies that there is only a single price which would satisfy the obligation.”<sup>32</sup>*

- 5.9. Secondly, Ofcom must have regard to the inherent discretion that Openreach has under a F&R obligation to set its own F&R charges taking into account a range of factors. Openreach has a degree of flexibility in setting prices of products subject to a F&R condition and it is entitled to price within a range of prices which might be F&R. In support of this, we further reference Ofcom's judgment in the MPF Dispute:

*“In considering TTG's case, i.e. that the consultation base case constituted the best available information on which to assess the Openreach MPF rental price (which we do not consider to be the case), we do not consider that Openreach, in maintaining the Openreach MPF rental price following publication of the March 2011 Consultation or November 2011 Consultation is not in compliance with SMP Condition FAA1.”<sup>33</sup>*

- 5.10. Thirdly, Ofcom must have regard to the fact that there is no set cost standard for assessing compliance with a F&R pricing obligation. In this regard, Openreach observes that in the MPF Dispute, Ofcom actually adopted a distributed standalone cost standard for MPF rentals.<sup>34</sup> Although that cost standard was in the context of a cost orientation obligation, there is no suggestion that it did not comply with the F&R obligation that, at that time, applied to MPF rental in tandem.
- 5.11. By fundamentally changing its approach to assessing F&R, Ofcom is interpreting the F&R obligation as being tantamount to a de facto charge control (see also paragraphs 7.3 to 7.9 of this submission below on the important differences between charge control and a F&R pricing obligation). This approach introduces significant uncertainty as to how the F&R condition should be interpreted and applied which, if maintained, is likely to lead to greater internal compliance costs and more disputes, particularly in relation to other situations where there is a lacuna period between charge controls. Moreover, and more generally, regulatory uncertainty and unnecessary regulatory intervention also have a chilling effect on investment and innovation, contrary to the best interests of LLU operators and end users.

***Ofcom can be confident that the current price is F&R***

- 5.12. Applying the established F&R principles in this case, Openreach is confident that the current MPF charges are not excessive or outside the range of F&R charges. The WLA Consultation sets out a range for MPF SML1 in 2020/21 between £76 and £91 per annum, a 20% range of +11% to -9% around its base case of £82. These ranges are set by reference to assumptions Ofcom has made in relation to, for example, volumes, Weight Average Cost of Capital (“WACC”), efficiency, both operating expenditure and capital expenditure, inflation (both pay and non-pay), service levels, cost volume relationships, and represent a reasonable range within which a charge control price might be set.<sup>35</sup>

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<sup>32</sup> MPF Dispute, paras 4.40 and 4.42.

<sup>33</sup> MPF Dispute, para 4.41.

<sup>34</sup> MPF Dispute, para 4.10.

<sup>35</sup> Indeed, this is usually the case and in previous market reviews, where a price for a product falls outside of a range, Ofcom has considered it necessary to re-consult.

- 5.13. Applying that range to Ofcom's proposed 2017/18 price of £84.38 results in a range of £77 to £94 per annum. BT's current price of £85.29 is well within that range. The fact that the current price of MPF SML1 sits comfortably within the extrapolated range for 2017/18 provides confidence that the current price of £85.29 is F&R.
- 5.14. Openreach is in the process of preparing its detailed response to Ofcom's charge control proposals in the WLA Consultation (which is due 9 June 2017), the very same analysis Ofcom relies on to formulate the Proposal for the Lacuna Period. It would be unreasonable to expect BT to be able to lay out its detailed comments on those proposals within an abridged timetable, half way through the WLA Consultation period. That said, and subject to and without prejudice to any more developed argument Openreach and BT might make in its responses to the WLA Consultation, Openreach considers Ofcom's proposed range and base case are too low.
- 5.15. In general terms, historically, it is unusual for Ofcom's consultation proposals for charge controls to remain the same at the end of the market review process. For example, in the 2014 FAMR consultation, the base case for MPF was CPI-0.75% whilst the control in the final statement was CPI + 0.30%. On that basis, it would be unrealistic for Ofcom to proceed on the assumption that the proposed prices/costs being consulted upon as part of the WLA Consultation will be the final, considered prices/costs.
- 5.16. More specifically, there are a range of issues where BT believes there is evidence to suggest Ofcom's base case costs are understated. If Ofcom corrected its analysis, in whole or in part, for these issues, it is entirely plausible that an MPF price increase will be proposed in the final statement for the WLA Market Review rather than a price reduction. An MPF price increase, which when extrapolated backwards would result in a price of £85.29 or higher in 2017/18 on Ofcom's own terms, is explicitly within the range that Ofcom is consulting upon. [REDACTED]
- (a) [REDACTED]
  - (b) [REDACTED]
  - (c) [REDACTED]
  - (d) [REDACTED]
  - (e) [REDACTED]
  - (f) [REDACTED]
- 5.17. The fact that Openreach has, even at this early stage of the WLA Consultation, managed to identify a number of issues suggesting that Ofcom's base case price is significantly too low, provides further comfort that its current pricing for MPF SML1 and the Commitment is well within a range consistent with the F&R condition.

## 6. THERE IS NO LAWFUL RATIONALE FOR THE PROPOSAL

- 6.1. In this section, we set out why there is no factual, legal or regulatory justification for Ofcom's Proposal. As a result, it falls outside the scope of Ofcom's lawful powers under the Act and the CRF.

6.2. So far as Openreach can make out, Ofcom's reasons for the proposal are as follows:

- (a) There is a risk of an adverse effect on competition because of BT's ability and incentive to engage in excessive pricing.<sup>36</sup>
- (b) If Ofcom does not take steps now "*there will be an extended period of uncertainty for industry at to the level of the fair and reasonable charge for MPF*" which may give rise to regulatory disputes.<sup>37</sup>
- (c) The F&R charge condition imposed in the 2014 FAMR does not provide "*sufficient protection on its own for such an important service, given BT's significant market power*".<sup>38</sup>
- (d) Ofcom therefore considers that it is appropriate "*to issue a direction to BT to specify a fair and reasonable charge for the provision of network access to MPF at SML1*", applying from the date on which it is put into place until revoked by Ofcom.<sup>39</sup>
- (e) The best information that Ofcom has is the model it has prepared for setting a charge control in the WLA Consultation and, although this model is still subject to consultation, "*it represents an appropriate basis upon which to ensure that BT applies a fair and reasonable charge for MPF SML1 at this time*".<sup>40</sup> Ofcom has therefore used the principles of its glidepath in the WLA Consultation to "*work back to derive a fair and reasonable charge*".<sup>41</sup>

6.3. Ofcom explains the legal basis for the Proposal as follows:

*"1.29. ... section 87(9)(d) authorises Ofcom to impose obligations by way of SMP services condition, to adjust prices in accordance with such directions given by Ofcom as they may consider appropriate. We propose to apply the direction making power in SMP Condition 1.2(b)(ii) to specify a fair and reasonable charge for MPF SML 1 within the meaning of Conditions 1.2(b)(i)."*<sup>42</sup>

6.4. For the reasons given below, however, Ofcom's proposal is neither consistent with its statutory duties nor meets the statutory requirements set out in the Act.

***No relevant risk of adverse effects from price distortion***

6.5. Ofcom proceeds on the mistaken basis that, in order to impose a specific charge for MPF SML1 during the Lacuna Period, it is only required to show that the new condition is justified by reference to the test set out in section 47(2) of the Act (as repeated in section 49(2)). That approach is misguided for the reasons given below. Moreover, and in any event, Ofcom has erroneously and unlawfully disregarded the requirements of sections 6 and 88 of the Act and the Access Directive, including the requirement to show a relevant risk of adverse effects from price distortion.

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<sup>36</sup> Consultation, para 1.16.

<sup>37</sup> Consultation, para 1.16.

<sup>38</sup> Consultation, para 1.19.

<sup>39</sup> Consultation, para 1.20.

<sup>40</sup> Consultation, para 1.22.

<sup>41</sup> Consultation, para 1.23.

<sup>42</sup> Consultation, para 1.29.

- 6.6. The Proposal imposes an obligation on BT to adjust its prices in accordance with Ofcom's direction for the purposes of section 87(9)(d) of the Act. Alternatively, it is tantamount to setting a price control i.e. a specific maximum charge for a product under section 87(9)(a). In either scenario, in accordance with the requirements of section 88 of the Act, an intervention of this nature, which is amongst the most serious forms of regulatory intervention, requires additional justification on the basis that, absent the intervention, there is a risk of adverse effects from price distortion. For the avoidance of doubt, BT's position is that Ofcom is not relieved of the burden of demonstrating (with reasons) that it has satisfied the conditions set out in section 88 of the Act and in the Access Directive when it imposes an obligation to adjust prices pursuant to a direction or a price control.
- 6.7. Ofcom has made no attempt in the Consultation to explain why it considers that the requirements of section 88 of the Act are satisfied in relation to the Proposal; it only sets out why the imposition of the original F&R condition (FAMR Condition 1.2(b)) back in 2014 was justified under section 88 of the Act.<sup>43</sup>
- 6.8. Ofcom wrongly attempts to justify its Proposal on the basis that it is necessary to ensure that the charge for MPF SML1 is F&R. But in terms of assessing the risk of adverse effects, it has totally ignored the terms of the Commitment offered by BT regarding the prices of MPF SML1 during the Lacuna Period, which are reaffirmed in this submission. That Commitment guarantees a charge which is F&R and derived from the regulated charge control for SML2 (see paragraphs 5.12 to 5.17 of this submission above).
- 6.9. Given that Commitment, and given the reasoning in paragraphs 5.12 and 5.13 in this submission above on why the WLA Consultation provides comfort that the current price is F&R, the MPF SML1 price is not set at an excessively high or unfair level. Nor is there any risk of distortion of competition between downstream operators or exclusion of their service offering. As such, Ofcom has not discharged its burden of proof under section 88 of the Act. In the absence of those requirements being satisfied, Ofcom does not have the power to impose the Proposal under the Act.

***No objective justification***

- 6.10. Ofcom's purported justification for the Proposal is that it is required to provide greater legal certainty and transparency for communications providers, and that the F&R condition is not sufficient protection by itself. That professed state of uncertainty is unsustainable in the light of BT's Commitment to maintain prices for MPF for the Lacuna Period. Ofcom's reasoning entirely disregards the Commitment offered by Openreach to fix prices at current levels, which would have provided certainty and transparency, and which would not involve simply relying on the F&R condition alone. That situation is unfortunate in circumstances where BT actively engaged with Ofcom, at the latter's request. Ofcom must explain why the Proposal is objectively justified notwithstanding the Commitment made by Openreach. Openreach submits that it cannot reasonably do so.
- 6.11. As to certainty, the publication of the Commitment on Ofcom's website has meant that all providers have been made aware of the precise charges well in advance of the end of the charge control on 31 March 2017. Openreach gave the Commitment seven months in advance of that expiry, providing absolutely certainty of the position. Further, Ofcom engaged in and published correspondence with LLU operators, including TT, regarding the Commitment so it is clearly in the public domain.

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<sup>43</sup> Consultation, para 1.27.

6.12. To the extent that there might have been any uncertainty as to the MPF SML1 price that was being offered by Openreach (and Openreach does not consider this to have been the case), Ofcom could have sought clarification from Openreach. In any event, Openreach has in this response clarified that Ofcom's understanding in this regard is correct and that Openreach has committed to a maximum charge of £85.20 for SML1 during the Lacuna Period. On the other hand, Ofcom's decision to introduce this Proposal with no certainty as to the date of the expiry of the proposed charge, or how providers are to treat the period between 31 March 2017 and implementation of the new charge, introduces considerable uncertainty that did not exist before.

***The Proposal is not necessary or proportionate and does not further end-users interests by reference to an appropriate counterfactual***

6.13. As to the sufficiency of the F&R condition, in FAMR 2014, Ofcom deliberately provided for a regime under which a F&R pricing obligation would apply by default at the expiry of the charge control. Ofcom has presented no evidence or reasoning to explain why it now considers that this fall-back position is "*not sufficient*", save for a vague allusion to BT's significant market power and loose references to BT's supposed ability and incentive to engage in excessive pricing (which indeed applied when the original F&R "fall back" condition was imposed by Ofcom in 2014). Those generalisations fail to take account of a number of relevant considerations, including:

- (a) the Commitment offered in relation to MPF, which means that BT's prices for MPF SML1 are "price-pegged" to the regulated cap for SML2. Insofar as Ofcom's approach assumes that Openreach would not set a F&R price absent the Proposal, BT vigorously disputes this. For the reasons given at paragraphs 5.12 to 5.17 of this submission above, Openreach is confident that its current price is F&R;
- (b) the fact that purchasers of MPF SML1 have other avenues to raise concerns about the compliance of the current MPF SML1 price with the F&R obligation (i.e. directly with Openreach) and resolving any disputes (by referring a dispute to Ofcom); and
- (c) the voluntary commitments provided by BT and Openreach as part of the Strategic Review in terms of Openreach's independent governance, with a new Openreach Board committed to operating Openreach in accordance with BT's regulatory obligations under the Act and to consider and address as appropriate representations for communications providers and other stakeholders.<sup>44</sup> These voluntary commitments also provide that the Openreach Executive will engage with customers (and other stakeholders, including Ofcom) to understand their requirements, demands, issues and concerns, and in a manner which treats all customers equally.<sup>45</sup> These arrangements reduce the ability and incentive of Openreach to engage in excessive, unfair or discriminatory pricing.

6.14. It follows that the Proposal is also contrary to Ofcom's general obligation to ensure that regulatory action is only targeted at cases in which action is needed,<sup>46</sup> and to carry out its functions with a view to ensuring regulation by Ofcom does not include "*the imposition of burdens which are unnecessary*".<sup>47</sup>

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<sup>44</sup> Governance Protocol, Part A, paras 2.18 and 2.24.

<sup>45</sup> Governance Protocol, Part B, para 4.1.

<sup>46</sup> Act, section 3.

<sup>47</sup> Act, section 6(1)(b).

- 6.15. Ofcom has not sought to assess its Proposal against the status quo or other realistic counterfactual to substantiate its concerns of adverse effects or demonstrate the actual difference that the Proposal would make in practice. Ofcom does not demonstrate that the Commitment or any other lesser form of intervention would achieve the same result without the need for a further intrusive *ex ante* SMP condition. It has not demonstrated that its Proposal is the most proportionate means of achieving its regulatory objectives. For the reasons given above, the Proposal is not necessary for, or effective in, achieving Ofcom's objectives of greater certainty and transparency, since the Commitment offered by Openreach in relation to the ongoing F&R condition also satisfies these objectives.

## 7. THE PROPOSAL IS INAPPROPRIATE

- 7.1. In this section, we set out further reasons why Ofcom's proposal to impose a direction setting the level of charge that is required by the F&R condition for MPF SML1 is inappropriate from regulatory and policy perspectives, and would further breach Ofcom's obligations under domestic and EU law.

- 7.2. In summary, it appears that:

- (a) Ofcom proposes to impose an obligation on BT to adjust its prices in accordance with its directions regarding what it considers to be the correct price for SML1. That is a SMP condition pursuant to section 87(9) of the Act, which cannot be set without observing the conditions in section 88 of the Act. Ofcom does not appear to have followed those steps or provided any reasoning as to why the imposition of the direction is necessary or appropriate.
- (b) Ofcom is actually proposing to conflate two separate SMP conditions with different purposes and outcomes i.e. a F&R pricing obligation and a charge control. This is inappropriate from a policy perspective and without proper legal basis.
- (c) Ofcom is attempting to impose a de facto charge control for the Lacuna Period without undertaking the necessary market analysis, contrary to its legal obligations and appropriate regulatory practice.
- (d) Ofcom has not established any risk of adverse effect (as discussed above).
- (e) Ofcom is effectively proposing the pre-emptive implementation of its projected WLA charge control which is expected to apply from 1 April 2018. This is a breach of the principle of non-retroactivity and presupposes the outcome of an ongoing consultation which raises serious legal questions about Ofcom's compliance with procedural requirements, due process and its wider regulatory obligations in the Act and the CRF.

***Charge control and F&R obligations are two separate SMP conditions with different purposes and outcomes and should not be conflated.***

- 7.3. A charge control obligation is an interventionist remedy by which the maximum price is set by a regulatory condition. Charge control is a specific remedy which is imposed in circumstances where it is considered necessary, reasonable and proportionate to direct a specified price or a glidepath over time to reach the desired price point. By definition, charge controls remove a substantial degree of pricing freedom and, as the most intrusive form of *ex ante* regulation, must only be imposed in exceptional circumstances where there is no effective competition

and where other less intrusive means will not be effective. This is made clear on the face of Article 8 of the Framework Directive and Article 13 of the Access Directive.<sup>48</sup>

- 7.4. Further, a charge control is cost based and relies extensive review of the prices and costs of a service at a future point in time. Given that those costs, and market conditions, change over time, and due to margin of error arising from such a forward looking analysis, it is very important restrict the charge control to a defined period i.e. 3 years. For these reasons, it makes perfect sense that Ofcom limited the MPF charge control to 3 years and designated that after that 3 years the relevant MFP rentals would be subject to a F&R condition.
- 7.5. In contrast, a F&R pricing obligation is not supposed to be such a rigid form of regulatory intervention. As set out in FAMR 2014, the F&R was imposed to address a relevant risk of adverse effects arising from excessively high prices<sup>49</sup> whilst allowing recovery of common costs.<sup>50</sup> It is intended to allow the network operator the ability to finance its activities, attract investment, invest in innovation and assess the appropriateness of its prices over time. At the time of the 2014 FAMR, Ofcom remarked that the F&R condition allows BT flexibility on pricing levels and does not impose cost-based price regulation.<sup>51</sup> In FAMR 2014, F&R is a general pricing obligation that applies to all regulated products that are not subject to a specific charge control. It is also enduring i.e. not time limited. On this basis, F&R is a general “fall back” remedy providing a base level of regulatory oversight of prices which, in the context of FAMR 2014, would apply to those products not considered necessary to be subject to charge control and those products where a charge control has expired.
- 7.6. Importantly, EU law recognises the difference between F&R and other price controls: Recital 22 of the Access Directive describes an obligation to ensure prices are “reasonable” as “relatively light” in contrast to more interventionist remedies such as cost orientation<sup>52</sup> (and *a fortiori* the more extreme charge control mechanism) which should only be used in escalation in proportion to the underlying competition problems.
- 7.7. Ofcom has itself recognised the important distinction between a F&R obligation and charge controls in the MPF Dispute (emphasis added):

*“There is, therefore, a distinction between an SMP Condition imposing a charge control and an SMP Condition relating to Network Access.”*

*An SMP Condition which imposes a charge control may specify a particular price and while such a price would be compliant with the requirement for network access to be provided on “fair and reasonable terms conditions and charges”, it may not be the only figure which would be compliant with the SMP Condition relating to Network Access (i.e. that would be a fair and reasonable charge).*

*TTG, in specifying a single price £90.00, have therefore assumed that the price is the only charge that would be considered to be “fair and reasonable” in the context of the SMP Condition relating to Network Access.*

*We do not agree with TTG’s view that only a charge of £90.00 (based on the information published in the March 2011 Consultation) would secure compliance with Condition FAA1.*

<sup>48</sup> See paragraph 4.4 of this submission above.

<sup>49</sup> FAMR 2014, para 10.36.

<sup>50</sup> FAMR 2014, para 10.83.

<sup>51</sup> See, for example, FAMR 2014, para 10.39.

<sup>52</sup> Access Directive, Recital 20.

*The charge control SMP obligation and the Network Access SMP obligation (and indeed also the cost orientation SMP obligation) are separate and designed to operate independently of each other. They are intended to provide ex ante regulation through different mechanisms. As explained above, we do not consider that the SMP Condition relating to Network Access, in the absence of a SMP Condition imposing a charge control, implies that there is only a single price which would satisfy the obligation.*<sup>53</sup>

7.8. Against this background, it is surprising that, in its Proposal, Ofcom conflates the concepts of F&R and charge control. It does this by proposing to direct the maximum level of a F&R charge which, on its face looks, and takes effect, like a charge control. Specifically, the Proposal states: “Unlike a formal charge control, which may set a specific charge following detailed modelling, identifying a fair and reasonable charge requires us to identify the best proxy from within a range of charges that may be fair and reasonable”.<sup>54</sup> In effect, Ofcom is using the Proposal as a means of imposing a charge control under the guise of a F&R condition.

7.9. There is no legal basis for this conflation. Ofcom is inappropriately cherry picking aspects of each SMP condition to construct and enforce an “informal” or “best proxy” charge control.

***Ofcom may only issue a direction or specify a price control, or a proxy price control, following appropriate market analysis***

7.10. Under section 86 of the Act, Ofcom may only impose a SMP condition (including a direction to adjust prices charge control) pursuant to section 87(9) of the Act, when it has: at the same time carried out proper analysis of the market and made a market power determination; or the condition was set by reference to a prior market power determination and Ofcom is satisfied that there has been no material change in that market since the condition was set.<sup>55</sup> This is particularly important to ensure that this most restrictive form of *ex ante* SMP regulation is fully justified.

7.11. It is clear from the Proposal that Ofcom has neither made, in accordance with the Act, a market power determination at the same time as the Proposal, nor reached a finding that there has been no material change in the relevant market since the last market power determination. The latter would be impossible. There have been notable changes since the 2014 FAMR, including the introduction of SML1 as a new MPF product, by Openreach and the migration by CPs of their services from SML2 to SML1. Further, BT has offered voluntary commitments in relation to the Strategic Review and, moreover, a specific Commitment regarding the pricing of both SML1 and SML2 for the Lacuna Period until the introduction of the next charge control. These are obviously material changes in the market which warrant a separate market power determination.

7.12. Given the considerable period of time that has elapsed since the last market power determination in 2014, and the obvious changes which have taken place in the market since then as discussed above, it is incumbent on Ofcom to carry out a proper market analysis before imposing a de facto charge control. Ofcom's failure to do so is a breach of the specific requirements of section 86 of the Act, and is, in any event, contrary to Ofcom's general

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<sup>53</sup> MPF Dispute, paras 4.28 to 4.31.

<sup>54</sup> Consultation, para 1.21.

<sup>55</sup> Act, section 88. See also paragraphs 2.17 and 4.5 of this submission above.

obligations to ensure that its regulatory activities are transparent, accountable and targeted at cases in which action is needed, and that it does not impose burdens which are unnecessary.<sup>56</sup>

***Breach of non-retroactivity and other procedural failings***

7.13. In this regard, Ofcom proposes “to adopt the base cases figures for MPF (SML1) on which we are consulting in the 2017 WLA Consultation...to apply the principles of our glidepath to work back to derive a fair and reasonable charge.”<sup>57</sup> Ofcom is in effect preemptively and retrospectively implementing a forward looking charge control methodology and prices that are still subject to consultation. This is an obvious breach of Ofcom's public duties to act in a manner which is procedurally fair and is contrary to Ofcom's own previous practice.

7.14. The approach taken in the Proposal was disavowed by Ofcom in the MPF Dispute. In that case, Ofcom considered a dispute brought by TT against Openreach to determine whether the price voluntarily set by Openreach for its wholesale MPF rental during a similar lacuna period was F&R. Ofcom summarised TT's demands as follows:

*“In effect, TTG is asking us retrospectively to set the Openreach MPF rental price for the period between 1 April 2011 and 31 March 2012 on the basis of our forward looking assessment relating to the charge control which is to apply from 1 April 2012. TTG argues that we should do this on the basis that the Openreach MPF rental price is not compliant with SMP Condition FAA1 (fair and reasonable) or SMP Condition FAA4 (cost orientation).”<sup>58</sup>*

7.15. In response Ofcom recognised:

*“TTG's premise seems to be that we have to use the information and analysis from the charge control consultation because it is the “best information currently available” and apply it to the Openreach MPF rental price. However, this would, in effect, be imposing a revised charge control on a retrospective basis in relation to a period that has already elapsed and notwithstanding that the future revisions have not yet come into effect. We note that it is settled law that we cannot apply an ex ante charge control with retrospective effect.”<sup>59</sup>*

7.16. It is remarkable that Ofcom is now taking the opposite approach by proposing to adopt an *ex ante* charge control with retrospective effect. That obviously inappropriate course is exacerbated by the fact that Ofcom has not even adopted the proposed charge control yet, since it is still subject to consultation. BT has not even had the opportunity to comment on those proposals or the underlying evidence yet. The Proposal also therefore unfairly pre-judges the outcome of the WLA Consultation, causing serious questions about the validity of that consultation process.

7.17. In addition, Openreach notes the following procedural flaws in Ofcom's approach to the Consultation:

- (a) Ofcom has failed to appreciate the inter-relationship of this Proposal and the main WLA Consultation and not allowed sufficient time to respond in full. Since Ofcom is proposing to set a F&R price by reference to its broader charge control price proposals as set out in the main WLA Consultation, Openreach cannot properly respond to the Proposal without assessing the methodology by which that price the MPF SML1 charge

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<sup>56</sup> See section 4 of this submission above.

<sup>57</sup> Consultation, paras 1.22 and 1.23.

<sup>58</sup> MPF Dispute, para 1.9.

<sup>59</sup> MPF Dispute, para 4.43.

has been set i.e. the charge control proposed in the main WLA Consultation. It is not feasible for Openreach to review the charge control methodology in the main WLA Consultation in just 5 weeks. It is usual for such a review to take at least 10 weeks, which is the time period afforded by Ofcom for Openreach to respond to the WLA Consultation.

- (b) Openreach observes that responding to this unforeseen, supplementary Consultation in tandem with the main WLA Consultation has strained resources designated to the main WLA Consultation. This may mean that Openreach cannot now meet the deadline for responses to the WLA Consultation.
- (c) The timing of the Consultation is unreasonably and plainly contrary to good regulatory practice. Ofcom has known for over one year that there would be a lacuna period during which Openreach would be subject to the F&R condition. Ofcom also liaised with Openreach from April to August 2016 regarding the terms of the Commitment. Whilst TT raised concerns with Openreach's Commitment following publication of the correspondence between Openreach, BT and Ofcom, an update in relation to the Commitment was published on Ofcom's website on 1 November 2016. Against this background, Ofcom has had ample time to resolve this issue and should not have published the Proposal on the very day that the charge controls expired. Best practice regulation would have entailed sufficient consultation (including with downstream customers and other stakeholders) in advance of the expiration of the charge control.
- (d) As well as for the reasons discussed in more detail above, where the nature and the consequences of intervention are particularly restrictive, the burden of evidential and analytical proof required to justify its proposed actions is particularly high. Ofcom has not undertaken or provided appropriate analytical or evidential proof to justify its Proposal, and the implicit decision not to adopt the Commitment offered by Openreach.

## **8. MODIFICATIONS TO THE PROPOSAL**

- 8.1. Without prejudice to the submissions made above, in the event that Ofcom implements the Proposal, there are a number of obvious gaps which must be addressed:
  - (a) Ofcom should include in the direction, a provision that the direction will come into effect at least 5 working days after the relevant final statement. This is because Openreach would need to take the price change through governance and load into our billing systems. This is consistent with how Ofcom generally imposes a charge control.
  - (b) Ofcom should include in the direction, a provision that the direction will expire on a specified date i.e. the date on which the new charge control is expected to come into effect (1 April 2018). Currently Ofcom's Proposal will apply until revoked by Ofcom. However, given that the direction is essentially a de facto charge control, Ofcom should set precise time limits and the direction should not be open-ended.
  - (c) Ofcom should include in the direction, a provision that allows the charge to be implemented without the 28 day notice period that would normally be required.
- 8.2. In addition, Openreach reiterates that the direction by Ofcom can only apply prospectively from the date that it is issued. As acknowledged by Ofcom in the MPF Dispute, as well as the Court of Appeal, *"it is settled law that we cannot apply an ex ante charge control with*

*retrospective effect*".<sup>60</sup> This means that from 1 April 2017 until such a time as a direction is issued, Openreach's only obligation with respect to MPF SML1 is to offer charges on an F&R basis. As above at paragraphs 5.12 to 5.17 of this submission, not only does Openreach consider that the charge offered in the Commitments meets those requirements but no evidence has been offered to the contrary.

- 8.3. Finally, Openreach reiterates that it is keen to continue constructive cooperation and would like to resolve any outstanding concerns that Ofcom may have through dialogue and cooperation without the need for intrusive and unjustified *ex ante* regulation.

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<sup>60</sup> MFP Dispute, para 4.43; Vodafone Limited, Telefónica O2 (UK) Limited, T-Mobile (UK) Limited and Orange Personal Communications Services Limited v. BT plc and Ofcom [2010] EWCA Civ 391.