Call for Inputs:
Narrowband Market Review

UKCTA Response to Ofcom

Submitted to Ofcom: 28th June 2012

UKCTA is a trade association promoting the interests of competitive fixed-line telecommunications companies competing against BT, as well as each other, in the residential and business markets. Its role is to develop and promote the interests of its members to Ofcom and the Government. Details of membership of UKCTA can be found at www.ukcta.com.

Introduction

UKCTA members represent the overwhelming majority of the UK's alternative fixed line sector and our members are acutely aware of the importance of this market review. UKCTA remains committed to ensuring that appropriate ex-ante regulation is maintained in situations where it is necessary to protect consumers from market failure. Reliance on ex-post regulation is not a substitute for appropriately targeted and proportionate remedies that are attuned to the specific needs of the UK market and consumers.

We have focused this response on the key areas of collective concern for UKCTA members, many of whom will be submitting their own detailed response to the Call for Inputs. The remainder of this response focuses on those specific issues.

Continued need for the Regulation of Single Transit Market

UKCTA is vehemently opposed to any deregulation of the Single Transit market. Transit is a vital wholesale market that enables all operators, regardless of size to offer a full range of voice destinations to end users. There are a number of instances where CPs are compelled to buy Single Transit from BT either as a result of lack of interconnection (where it would not be cost effective to connect to every other CP) or through BT bundling Single Transit into other products (NTS, Number Portability etc) and there are many sections of the market which are not competitive (in particular the many thin routes carrying traffic to smaller CPs which aren't expected to be benefit from competition).

The characteristics of the UK Single Transit Market are sufficiently different from other member states to warrant retention of SMP. The UK narrowband market has a large number of very small providers and an SMP transit product is required to provide end to end connectivity. UKCTA believes the UK transit market requires SMP on single Transit and comfortably continues to meets the three criteria test, with little if any change in the situation when it was last reviewed in 2009 having taken place.

The provision of network access on reasonable request is essential if end users are to enjoy cost effective seamless services from their communication providers. BT is interconnected with nearly all UK CPs, and the very few CPs who don't connect directly with BT rely upon other CPs who are, with BT refusing to pay any kind of transit fee to intermediate CPs in these instances, underlying the strength of the market power BT retain. The nearest competitor in the transit market is a long way behind and in reality due to the economics of interconnection is unlikely to challenge BT's position during the life of the next review. There are many bottlenecks in the market due to the scale of investment needed to connect directly to the many small providers who terminate UK number ranges.

It is essential that BT is not able to discriminate in the transit market. Without this protection BT could take action which might undermine the commercial interests of its competitors, by charging more for routes where no commercial alternatives are available. The unregulated market for GNP/NGNP transit between range-holder and recipient acts as a good indicator of BT's likely behaviour on uncontested routes to smaller CPs should regulation be removed, because it is inherently only used where either the range-holder or recipient is small so direct connection is uneconomic. It is notable that BT's pricing in this market is approximately three times that of the regulated transit market.

Ofcom's light touch approach to remedies in the Single Transit has worked well, giving BT the freedom to price as it see fits, yet through the imposition of the no undue discrimination obligation BT can't exploit its market power over the large number of uncontested routes where no alternatives are available.

Under Ofcom's proposals for Transit in the current NGCS consultation responsibility for paying transit in the NTS market would fall to entirely to the terminating provider, thus increasing the volume of compulsory transit that CPs must purchases from BT. Terminating CPs can do little to avoid this cost, as the originating provider does not control the routing of this traffic type.

Number Portability - APCCs

One of the concerns with single transit is that it is an unavoidable service when a call is routed via the BT network for termination on the recipient operator's network because the number has been ported. If the call is handed over to BT at the tandem layer, the average porting conveyance charge (APCC) is effectively the single transit charge.

The recipient operator has no way of avoiding this charge even if they interconnected directly with originating operator because of the way in which number portability currently works in the UK. The originating operator would always need to route the call to BT in line with the number portability routeing rules. In this context, it is a fallacy to argue that single transit is a cost that can be avoided through direct interconnection. The recipient operator does not have this option.

Ofcom has previously argued that the APCC is regulated separately through GC18. It is true that this provision requires the APCC to be fair and reasonable but we would nonetheless be concerned if SMP regulation was lifted from single transit because it would give BT freedom to increase its charges without any external insight as to the justification for such increase. This would inevitably have an impact on the level of the APCC and quite possibly trigger a dispute that would need to be resolved by Ofcom. Additionally, the APCC calculation itself is somewhat shrouded in mystery and seems to change regularly which denies operators regulatory and commercial certainty in trying to make these call scenarios as efficient as possible.

Number Portability – porting differential

A side-effect of the benchmark geographic termination rate for altnet operators being set at the BT LES rate is that overall BT will make a windfall gain on GNP. As range-holder network BT charges originators its own termination rate, and pays recipient networks based on the recipient termination rate. BT's net rate across all originators will be a blend of Single Tandem Termination and LES (we believe this to be of the order of 25%/75%), while the recipient rate will be LES. In all cases the APCC will recover BT's costs as range-holder, so BT will be left with a windfall gain where they are receiving STT, i.e. in 25% of cases.

BT would undoubtedly assert that this simply reverses the historic situation, where altnet rates were a blend of LES and STT so they faced a porting differential loss. This does not stand up to scrutiny, however: for Single Switch Operators, each individual altnet's blend of LES/STT rate was set according to the level of traffic they originated to BT at each rate, so it follows that in broad terms that in aggregate the blend that BT received at LES/STT will be what it out-paid at LES/STT. The only exception to this was Multi-Switch Operators, but even for these any out-payment made by BT in excess of that blend was entirely down to their performance in failing to route calls to the appropriate termination switch.

This issue requires examination, with potential consideration to BT passing through revenues in excess of the benchmark termination rate.

Need for a UK-wide Call Origination Remedy

The advent of LLU investment may mean some exchange areas have more choice of access competition, doubtless leading to BT urging Ofcom to adopt a geographic market approach similar to the WBA market. UKCTA is firmly of the view that the UK market for narrowband voice is a national one, requiring a national approach to wholesale remedies. While there are undoubtedly parts of the country where retail competition is more intense, the need for national wholesale remedies is as strong as ever in order to support choice for a broad range of consumers. A fragmented approach to regulation in the wholesale market for voice will greatly undermine consumer choice and harm the development of the market as the ability of key suppliers will be impaired. Ofcom should be very cautious about making any comparisons with WBA as the realities of the narrowband market are very different. While Broadband/Pay TV/Broadband bundled offerings are increasingly popular, there are a large number of consumers who choose to buy their services separately, which often results in them having access to a smaller range of suppliers. If the market were to fragment, the reduction in the addressable market would be such that many suppliers would either choose to exit it entirely, or only serve specific geographies, harming the interest of consumers in the long run.

CPs are unlikely to invest in multiple order systems and in-life management system to interact with a range of suppliers should BT's obligation for universal call origination fall away. Indeed there is every likelihood that those alternative providers who are not obligated to offer services would not do so, having no inclination or incentive to open up their infrastructure to other suppliers and no wish to incur the costs of developing a suitable wholesale product.

Consumers currently enjoy a wide range of supplier choice as many CPs and resellers utilise WLR & CPS and compete directly with LLU and other self-providers for retail telephony. If WLR/CPS providers were no longer able to offer service in particular areas then consumer choice would be severely restricted, leaving just a small number of self-supplying providers, some of whom may not offer telephony outside a broadband and/or Pay TV bundle.

Ofcom need to give careful thought to both the practical implementation issues of a geographic market approach and the unintended consequences for any other related markets. There is a practical mismatch between the DLE exchange footprints for voice services and the footprints of LLU providers, with LLU providers only having partial coverage within many DLE areas. This would lead to complexities when defining any market boundaries making a geographic approach extremely difficult.

There is an important issue in relation to the way in which markets interact with each other that must not be overlooked. If BT's call origination obligation was to fall away in certain exchange areas then the DLE interconnect routes used by many CPs may no longer be economically viable, resulting in them being removed, which in turn would increase BT's market power in related markets such as local-tandem conveyance, and could result in regulation being re-introduced for these services as the number of directly connected DLEs falls.

Notice Periods[1]

The finding of SMP, in itself, is not necessarily a suitable indicator of what is an appropriate notice period or not. It can only be reasonably considered in conjunction with a consideration of the whole supply chain for the entire basket of voice services consumed by End Users as well as on the basis of fairness, reasonableness and reciprocity.

[1] The views expressed in this section do not reflect the views of TalkTalk who will be submitting its own response to this consultation

UKCTA

Given that the 2009 EC Recommendation discusses symmetry in terms of rate setting, whilst silent on the topic of notice periods itself, it is reasonable to consider that symmetry in notice periods is the obvious corollary of any recommendation in rates.

End Users generally demand 30 days' notice – or one calendar month. Given that Ofgem, in 2011, mandated 30 days' notice of consumer price changes to avoid consumer harm, this feature of the end user to utility company relationship would appear to be rather entrenched. Therefore, it is reasonable to assume that the supply chain itself needs more notice than this (a supply chain which can be as long as Lead Network, Reseller, Dealer and sub-Dealer *in extremis*). BT currently only gives 28 days' notice on products that are unregulated or deregulated. We have no choice but to give them 56 days' notice under the Standard Interconnect Agreement (this differential is in part a historic issue to do with paper based price books) and they are required to give us 90 days for products under the Network Charge Control.

Any reasonable bystander will conclude that this is not fair, symmetrical or equitable, either in itself or in consideration of the wider context. SMP conditions, such as the Network Charge Control, have the benefit of being relatively predictable and can be forecast by reasonably knowledgeable persons within the industry well before the due date, whereas unregulated and deregulated ones cannot.

Therefore, the risk to consumers of reducing the 90 days to 56 days (with 14 days to turn around transit notices by BT, which is still a requirement) is far less potentially detrimental than leaving 28 days untouched, as this is less than the notice to consumers.

Where a Communications Provider takes on such risks, it may seek to protect itself by introducing a risk premium in its pricing – i.e. inflating the prices to compensate for the perceived risk in not having back-to-back notice periods in its wholesale arrangements. This is clearly not in the consumers' interest.

Given that the majority of the industry (including all UKCTA members and BT) are apparently aligned on a reciprocal 56 day notice, we hope that BT will agree to amend the appropriate clauses and schedules of the SIA to reflect 56 days' notice and that Ofcom will reduce the SMP condition commensurately on receipt of the appropriate guarantees.

There is one administrative problem, regarding the need to turn around individual CP price change notices to BT that are dependent upon their own price changes (e.g. the Benchmark Fixed Termination Rate, or keeping 056 LIECS pricing aligned to Geographic as is the convention some follow) but these are far from insurmountable and it is our understanding that BT has committed to work with industry to resolve these hurdles.

Finally, we must stress that all other reviewed markets have completely different consumer dynamics, therefore any comment we make regarding acceptable Notice Periods herein, is, of course, restricted wholly to this Narrowband market only.

Non-Geographic Call Termination

UKCTA considers that Ofcom should take this opportunity to review the market for non-geographic termination services alongside its proposed review of the market for geographic termination.

There is currently a regulatory asymmetry between the treatment of termination of wholesale geographic and non-geographic calls in the UK. Geographic termination is regulated with all terminating CPs designated as having SMP, whereas non-geographic termination is not regulated, the only review of the market having been abandoned at the consultation stage in 2004 and never completed.

This asymmetry has come into sharper focus since the last narrowband market review, when Ofcom maintained its split definition between the geographic and non-geographic wholesale termination markets. Since that time BT has progressively increased non-geographic termination charges through a series of NCCNs introducing ladder pricing, which has resulted in multiple disputes being brought from 2009 onwards. None of these disputes have provided any regulatory certainty, with all dispute determinations having been appealed, and no appeal having been finally concluded. The introduction of ladder pricing has demonstrated that BT can unilaterally impose a pricing structure for non-geographic termination. Additionally, the lack of certainty over whether these rates are acceptable in the absence of ex ante regulation is potentially affecting the functioning of this market to the detriment of other communication providers and end users.

The Commission still regards wholesale termination as a market susceptible to ex ante regulation, it appears as market 3 in its Recommendation on relevant product and service markets ('the Recommendation'), and it is significant that there is no distinction between the termination of geographic and non-geographic calls. The Recommendation is clear that "*national regulatory authorities should analyse the product and service markets identified in the Annex*". Ofcom have failed to undertake any analysis of this market, and therefore have not followed the Recommendation. NRAs are required to take utmost account of the Recommendation, and at the very least Ofcom is obliged to set out full reasons as to why it has chosen to adopt a different course to that set out in the Recommendation. From the failure in 2004 to conclude their first market review, Ofcom have failed to do this, and as such there appears to be a procedural failing in this regard.

UKCTA members remain fully engaged with Ofcom's current Simplifying Non-Geographic Numbers review, which seeks to review NTS services as a whole. However, as Ofcom is at pains to point out, this on-going review is not a competition based assessment of a market (and certainly not the non-geographic wholesale termination market), and as such, whilst there is some overlap, its aims and objectives are wholly different to the function of a market review. Additionally, the timing of the Simplifying Non-Geographic Numbers review is such that any implementation of proposals are likely to be at the end of the proposed forward look period for this Market Review, even assuming the currently proposed timetable holds. The existing call origination condition should remain in place until such time as the new regime is in place.

UKCTA believes that there is a need to undertake a review of the wholesale non-geographic termination market and that this should form part of the forthcoming narrowband market review. Such a review is required to comply with Community obligations derived from the Recommendation and to address the increasing problems that exist and are continuing to develop within this market.

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