# OFCOM'S REVIEW OF THE FIXED NARROWBAND SERVICES MARKETS - CONSULTATION ON THE PROPOSED MARKETS, MARKET POWER DETERMINATIONS AND REMEDIES

**Response by British Sky Broadcasting Limited ("SKY")**

## EXECUTIVE SUMMARY

1. This is Sky's response to Ofcom's consultation on the review of the fixed narrowband services markets ("NMRC").[1]

2. Sky considers that a Next Generation Network ("NGN") should be treated as the modern equivalent asset ("MEA"). This is evidenced by all recent market entry being NGN based and legacy equipment no longer being available. Ofcom's proposed reversal of its original position[2] (that the NGN is the MEA) does not appear justified or proportionate and, in any event, is not a neutral decision in that it will continue to incentivise legacy operators not to invest in newer more efficient technology, introduces unnecessary costs for NGN operators and deprives consumers of the benefits of more effective competition.

3. While Ofcom has provisionally stepped away from adopting a NGN as the MEA, it is proposing to base the network charge control ("NCC") upon NGN costs and, in the case of wholesale call termination, is setting prices on the basis of pure long run incremental costs ("LRIC"). This is a departure from Ofcom's current approach where it bases the NCC on a hypothetical on-going (legacy) network which inflates BT's actual costs. Sky considers that it would be inconsistent to adopt this new approach whilst allowing BT's average porting conveyance charges ("APCCs") to be set by reference to legacy network costs with a mark-up for common costs. Sky considers that in these circumstances, the APCC can no longer be considered to be cost oriented (even if they could be before) as they are required to be under General Condition 18.

4. The conditions in relation to the Single Transit market are not materially different today to those at the last narrowband market review where Ofcom found BT to have SMP. This was because BT, uniquely, interconnects with all networks in the UK

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1 Review of the fixed narrowband services markets – consultation on the proposed markets, market power determinations and remedies dated 5 February 2013.

2 Ofcom, Narrowband Market Review – Consultation on possible approaches to cost modelling for the Network Charge Control for the period 2013-2016 dated 28 September 2012 ("September Consultation").

and, in part, is able to do so due to its scale and its end-to-end connectivity obligations. Given that there has been no material change in the market conditions and the conditions are unlikely to change over the market review period, Sky considers that it remains appropriate to find that BT has SMP in Single Transit and require it to offer such services on a regulated basis.

5. Ofcom's proposed 12 month sunset clause for the removal of the obligation on BT to offer Indirect Access ("IA") and, when not coupled with WLR, Carrier Pre-Selection ("CPS") does not allow communications providers ("CPs") sufficient time to make alternative arrangements where required (due to product withdrawal or changing commercial rates). There are significant established services and equipment which make use of IA and CPS without WLR and, therefore, Sky considers a 24 month sunset clause would allow a more appropriate period during which alternative mitigation plans can be invoked.

**NGN IS THE MEA**

6. Sky considers that setting prices on the basis that a NGN is the MEA is long overdue. It is appropriate, in part, because NGNs are sufficiently proven to enable Ofcom to adopt this approach.

7. As set out in Sky's response to the September Consultation[3], in Sky's view, it has long been apparent that NGNs are the efficient method for supplying fixed line voice services on a national basis. This is evident from:

    a) BT's original 21CN plans; and

    b) the wide-scale roll out of NGN based voice services by Talk Talk and Sky to their subscribers.

8. Sky recognises that the original decisions by some CPs to invest in networks based on time division multiplexing ("TDM") may have been the efficient choice at the time.

9. However, this can no longer be relied upon to form the basis of regulation of narrowband markets where Ofcom has a responsibility to promote competition and efficiency. Adopting NGN as the MEA now will send the right investment signals and incentivise CPs to make more efficient technology choices. Furthermore, this choice will also be consistent with Ofcom's duty of technology neutrality[4] as Ofcom is not favouring one technology over another but simply recognising that NGNs are more efficient and that NGNs are the optimal network choice.

10. Ofcom's provisional decision now to depart from its earlier proposal and not identify NGNs as the MEA will shelter TDM operators from effective competition from efficient new entrants and, as a result, send the wrong investment signals to CPs. This is because legacy operators will not be required to offer internet

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[3] Sky response dated 19 November 2012 (the "September Response").

[4] Section 4(6) of the Communications Act 2003.

protocol ("IP") interconnection (or otherwise incur conversion costs) at local termination rates and at fewer locations nationally as they would if call termination markets were competitive thereby inflating the costs of NGN operators, like Sky. To argue that it is not clear that a NGN is the MEA because TDM operators do not seek IP interconnection when purchasing call termination from other networks misses the point – TDM operators' preferred method of interconnection is inefficient and only viable because of Ofcom's approach to regulation of fixed narrowband markets.

11. New entrants only deploy NGNs and the efficient method of interconnection is IP based. TDM networks are no longer efficient which is apparent given that new TDM equipment is no longer available.

12. Moreover, to allow the recovery of TDM costs by BT (and, by extension, by other legacy network operators) does not reflect the outcome in a competitive market and, as such, will dis-incentivise BT from ever fully migrating to a NGN because it will be able to earn more from continuing the legacy equipment and functions in its network than not.[5]

13. Sky notes that Ofcom also seeks to rely on two primary reasons in reaching its provisional decision not to identify a NGN as the MEA[6]:

- **Not all voice-related services are replicated using NGNs** – Ofcom identified that some call services (ISDN 30 and CLI based services) are not fully supported on NGNs and that physical interconnection via IP remains nascent in order to argue that it is premature to adopt NGNs as the MEA. Sky disagrees with this, there has been widespread adoption of NGNs, IP interconnection is mature and standards have been and continue to be developed. Indeed, even BT offers an IP interconnection product of sorts[7]. Furthermore, NGNs support all major call services. Those services cited as not being supported are often legacy services that have modern equivalent substitutes based upon the NGN (such as ISDN 30). Services which have no NGN-based substitute are likely to be relatively trivial (otherwise a NGN based solution would have been developed) and may only persist because TDM operators continue to be rewarded for sustaining their networks. It would be disproportionate and unreasonable to use these as a basis for not adopting a NGN as the MEA.

- **Robust comparison of the replacement costs of TDM networks and NGNs is very difficult –** While it is unclear that such a comparison is required, assessing these costs is not as difficult as Ofcom makes out given that its approach to setting the current NCC establishes the costs of a

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5 This is especially true if those legacy charges continued to be based upon Ofcom's anchor pricing approach whereby the legacy costs were modelled as if they were part of a hypothetical on-going network.

6 Paragraph A11.80 of the NMRC.

7 Although it is not offered on terms that are as attractive to NGN operators as those described in §10 above.

hypothetical on-going TDM network whereas, for the next NCC, Ofcom will adopt a NGN cost basis. Moreover, Ofcom claims that the difficulty arises, in part, as a result of the dearth of available data for new build TDM networks. It would be illogical not to adopt a NGN as the MEA because the costs of the legacy network are no longer known given that the equipment is no longer manufactured and no new networks are built based on the old technology. It is precisely because of this set of circumstances that Ofcom would be justified in adopting a NGN as the MEA.

## AVERAGE PORTING CONVEYANCE CHARGES

14. As stated in the September Response, Ofcom's current reciprocity guidelines[8] break with the long held reciprocity arrangements and, as a result, have allowed BT to introduce lower termination payments to operators like Sky who do not interconnect with BT at the local layer while maintaining higher charges when selling call termination to Sky. This has resulted in Sky being disadvantaged relative to locally interconnected operators even though it is inefficient for Sky to invest in local interconnection.

15. Furthermore, the impact of the new lower LRIC-based fixed termination rates ("FTRs") now proposed by Ofcom will be even more pronounced on Sky given that BT's current APCCs will be greater than this rate. As a result, Sky could not make a loss for every minute of traffic it terminates for a ported-in number which incurs BT's APCC.[9]

16. Whilst, as Ofcom acknowledges, the APCC is not formally part of the NCC, it is governed by the General Conditions and is required to be cost oriented under General Condition 18. In the NMRC Ofcom considers that APCCs are commercially negotiated and that this remains the most appropriate way for CPs to set APCCs.[10]

17. Sky considers that it would be inconsistent to set termination revenues by reference to pure LRIC and NGN costs while allowing the APCC to be set by reference TDM costs (and, possibly, even those of a hypothetical on-going TDM network) with a mark-up for common costs. Accordingly, Sky considers that Ofcom, noting the cost orientation obligation under GC18, should provide further guidance on the appropriate level of APCCs so as to avoid this imbalance.

## SINGLE TRANSIT

18. Sky considers that it remains appropriate to find that BT has SMP in Single Transit and require it to offer such services on a regulated basis. The conditions in relation to the Single Transit market are not materially different today as they were at the last narrowband market review where Ofcom found BT to have SMP and they are unlikely to change over the market review period. This is because BT, uniquely,

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8 Ofcom's guidance on Fair and reasonable charges for fixed geographic call termination (27 April 2011).

99 **[Confidential]**

10 Paragraph 8.117 of the NMRC.

interconnects with all networks in the UK and, in part, is able to do so due to its scale and its end-to-end connectivity obligations.

## CPS AND INDIRECT ACCESS

19. Ofcom has proposed to remove the obligation on BT to provide CPS and IA to CPs.[11] [**Confidential**] Ofcom proposes to allow a 12 month sunset period. Sky considers that this does not allow CPs sufficient time to make alternative arrangements where required (due to product withdrawal or changing commercial rates). Therefore, the sunset provision should be extended to 24 months to allow time for CPs to find alternative solutions and/or enter into discussions with BT about the continued provision of the required services.

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[11] Sky notes that Ofcom proposes to maintain the obligation on BT to provide CPS to an external CP who also purchases wholesale line rental ("WLR").