



Vodafone's response to Ofcom's consultation

"Draft Annual Plan 2013/14"

February 2013

Non-confidential

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Summary and conclusions

Vodafone welcomes the opportunity to comment on Ofcom's draft Annual Plan for 2013. Following Vodafone's recent acquisition of Cable & Wireless Worldwide it is the UK's leading integrated communications provider, hence a key stakeholder in Ofcom's activities.

We consider that, given the far-reaching changes and industry trends Ofcom notes in this document, Ofcom should take this opportunity to holistically review the state of competition in the UK telecommunications market. Nearly a decade after the Telecoms Strategic Review, we believe the time is right for another fundamental review. While we support the overall system of Market Reviews, there is an obvious difference between a market undergoing rapid technological and user change (such as Business Connectivity with its transition from TDM products to Ethernet and the emergence of distinct demand for mobile backhaul) and market where the underlying reality is more stable (such as mobile termination rates). Adopting the same review period for these two categories of markets makes little sense.. Moreover, examining market siloes means complex interactions between markets can be overlooked.

We believe that the key issues for Ofcom to consider in any such fundamental review should include:

- What forms of consolidation and convergence within the market would be consistent with competition and deliver good outcomes for consumers?
- In what concrete ways can Ofcom support efficient investment in infrastructure given its fundamental role underpinning the whole communications value chain?
- What regulatory rules or incentives should Ofcom introduce to counter non-operator barriers to switching including proprietary platforms, content rights and commercial bundling strategies?

Our other main concerns revolve around spectrum, next generation access and competition law enforcement.

Vodafone also considers the Draft Plan is of limited value in resource planning, without detailed dates to assess which stakeholder expertise will be required, and when. When releasing future Draft Plans, we believe Ofcom should include details of its expected dates for implementation so that stakeholders can comment on the interdependencies between different issues.

1: Need for a strategic outlook

It is now nearly a decade since Ofcom carried out the Telecoms Strategic Review. The TSR was a fundamental piece of work that resulted in real change with the creation of Openreach and BT signing up to a series of regulatory Undertakings. Since then, there has been considerable technology development via the deployment of Next Generation Networks and Next Generation Access and an acceleration in the shift from copper to wireless and fibre. These changes make Openreach's services even more vital, but the time since the TSR has seen the Openreach model and the undertakings gradually eroded..

Against this backdrop, Vodafone finds it surprising that the draft Annual Plan solely focusses on issues within the current framework, rather than additionally considering whether it is time to take a step back and determine how well the model is working to deliver sustainable investment and competition and whether technological change has moved bottlenecks within the value chain.

- We are particularly concerned that the nature of current regulation means that Openreach is only incentivised to operate at lowest possible cost, as any efficiency beyond charge controls increase its profitability. Regulation should seek to deliver the best overall service experience, which is a balance of price and quality. Ofcom needs to work with stakeholders to provide the correct incentives to Openreach to achieve this.
- The evolution to Next Generation Access architectures has in some cases (FTTC) moved the point at which it is possible to physically unbundle towards the customer, and in others (FTTP) made fibre unbundling potentially impossible. This has practical implications for the economic feasibility of continuing physical unbundling into an NGA environment, and hence the search for alternatives such as VULA moves Openreach further up the value stack into provision of bitstream services and active electronics; something not foreseen at Openreach's creation.

In addition to these trends, Ofcom makes a number of striking findings which merit a fundamental review now.

First, Ofcom recognises that the industry is meeting increasing consumer and investment demands in an environment of falling revenues:

- Customers are rapidly connecting more and more powerful devices to telecommunications networks. Smartphone ownership is up to 39% of UK adults with tablet ownership up to 11% and connected TV ownership up to 15%. UK consumers consume more data per mobile connection than any comparator country.¹
- At the same time, 2011 marks the third year of reducing revenue for the UK telecommunications industry as a whole with a drop of 1.9% this year.

¹ International Communications Review December 2012 at p. 9

- *“The growth in use of online communications services may affect the minimum quality of service required to engage effectively with communication services.”²*

This combination of developments goes to the heart of what level of coverage and capacity we should expect from telecommunications networks in the future. As more services move online including not just commerce and product-comparison but also e-government and the delivery of public services, Ofcom correctly identifies that increasing quality and capacity of telecommunications networks is required for consumers to effectively engage with wider society. In February 2012, Ofcom’s Communications Market Report valued online retail sales at £2.6bn, a year-on-year growth of 30%. In the past three years, e-commerce has grown at ten times the rate of other retail sales. Internet traffic on mobile networks is growing 84% year over year, while on fixed access Ofcom foresees an increase in 30% in lines using broadband and a fourfold increase in peak demand per line over the next decade³. However, despite the increasing need for capital investment, forecasts suggest that revenues will remain flat even as traffic increases. Clearly increasing investment to meet higher quality, speed and coverage demands in the face of falling revenues cannot continue in perpetuity.

Ofcom notes that in response to this investment environment *“network consolidation and convergence trends continue”⁴*. We believe Ofcom should take the opportunity of a Strategic Review to provide greater guidance on what forms of consolidation and convergence it considers beneficial to consumer outcomes. In particular, infrastructure sharing and spectrum pooling are identified in the European Commission’s recent “Action Plan on Wireless Communications for a Connected Europe” as areas where guidance is required.⁵ We believe that, given the UK’s advanced position in considering some of these issues (e.g. Ofcom’s review of MBNL and CTIL network sharing ventures) Ofcom should take an active role in shaping this guidance or issue UK-specific guidance itself.

² Draft Annual Plan at 2.9.

³ Narrowband Market Review February 2013, Figures A12.5 and A.12.6

⁴ Draft Annual Plan 2013/14 at 2.26

⁵ February 2013 *“Recent studies have identified the possibility for significant cost savings through infrastructure sharing and several Member States have developed first guidance in this regard. Therefore the action plan will explore the framework conditions for the deployment of mobile and wireless broadband infrastructure, considering for instance guidance (soft law) on infrastructure sharing, including the possibilities for spectrum pooling between operators.”*

Second, Ofcom notes the continued emergence of over-the-top platforms and services⁶ which both compete with and rely upon the infrastructure of vertically integrated players. Capital expenditure on connectivity represents 72% of the total capital expenditure within the wider e-commerce market.⁷ Again, Ofcom correctly identifies that without continued investment, the UK could end up with an insufficient quality of infrastructure to support this service innovation and competition:

- *“In many ways, infrastructure underpins the other elements of the value chain – it enables content and service delivery and as convergence continues it is increasingly relevant to a wider range of devices.”*
- *“The demands placed on the UK’s infrastructure are increasing as consumer demand for data grows.”*⁸

Ofcom should expressly recognise within its strategy that it has a positive duty to promote efficient investment and innovation in new and enhanced infrastructures.⁹ This means maintaining a regulatory environment which encourages investment while tightly scoping bottleneck capabilities and secures access to them for competitive stakeholders on an equitable basis across all customer sectors. Ofcom also needs to ensure that operator technology choices (e.g. FTTC vs FTTH) are future-proof and do not restrict competition. Ofcom should also work with other stakeholders to lower or remove barriers to the rapid deployment of telecommunications networks.

Third, there are strong non-operator barriers to consumer switching such as content rights, bundled offers and device operating systems.

- *“Portability of content across devices is now considered a basic expectation by some consumers and the demand for such flexibility in use may become commonplace in the future.”*¹⁰
- Some operating systems are specifically tied to devices while others are more open. *“Both models may represent challenges to policy designed for more traditional platforms.”*¹¹
- 19% of UK homes have a triple-play bundle of fixed voice, broadband and multichannel TV.¹²

Ofcom currently proposes to *“implement policies that will improve the ease of switching between communications providers.”*¹³ We believe it should broaden this work to consider non-operator barriers to switching including content rights and proprietary operating systems.

⁶ Draft Annual Plan 2013/14 at 2.62

⁷ http://www.atkearney.com/en_GB/paper/-/asset_publisher/dVxv4Hz2h8bS/content/the-internet-economy-in-the-united-kingdom/10192

⁸ Draft Annual Plan 2013/14 at 2.18

⁹ Framework Directive Art. 8(5)(d) and S.134 of the Communications Act 2003.

¹⁰ Draft Annual Plan 2013/14 at 2.8

¹¹ Draft Annual Plan 2013/14 at 2.60

¹² Draft Annual Plan 2013/14 at 2.6

¹³ Draft Annual Plan 2013/14 at Figure 1

2 : Do market reviews mask competitive weakness?

Vodafone supports the approach of Market Reviews, from which regulation follows where required. We do however query whether a static review period should be adopted as is the case now, versus a more dynamic approach dictated by the pace of market and technological change in a given market.

Further, we have concerns that the siloed approach of looking at markets as defined at a European level could mask pan-market considerations and obscure the bigger questions over what is required for the consumer. In particular, we have concerns that individual Market Reviews could find that a given Communications Provider does not have significant power in each of the markets, but there could be a combinatorial effect, in that it is only when the weaker power in each is taken in aggregate that an overall market power becomes clear.

For example, Ofcom has held that BT does not have market power in various wholesale markets such as (non-single) transit voice, leased lines and broadband access in Market 3 areas. Notwithstanding these findings, its ability to holistically serve these markets give it a unique position over those providers who are unable to realistically operate in all of them.

These inherent efficiencies of scope means that wholesale customers could prefer to deal with them as a single supplier, thus distorting the overall market in a way not detected by individual market reviews. These potential failings at a wholesale market level could well have implications for competition at the retail level, thus impacting consumer outcomes.

3 : Competition Act Investigation handling

We are very concerned that the length of time taken to assess Competition Act investigations means that stakeholders are being put off bringing issues to Ofcom, thus harming competition. We welcome the fact that Ofcom published guidance in 2012 on timelines for competition law investigations thereby increasing market certainty.

However, we note that Ofcom is still to reach a conclusion in the Wholesale Calls Margin Squeeze Competition Act investigation. This case was opened four and half years ago with a Statement of Objections produced over two years ago. The length of time the case has taken is unacceptable and in itself acts as a barrier to effective competition, as the threat of securing effective competition enforcement action has diminished due to Ofcom's track record in these cases. Ofcom must look closely at its processes and resourcing to bring about improvement and ensure that is able to act as a competent competition authority for the industry.

4 : Impact of technology choice on regulation

In NGA, we note and welcome Ofcom's review of Openreach products against the VULA requirements, which we will comment on further below. However, we believe that more strategic consideration should be given by Ofcom as to whether the

technologies deployed by Openreach are capable of supporting a long term pro-competitive NGA market.

Whilst a fit-for-purpose VULA proposition is to be supported in the near-term, it is likely that the long term model which will provide the most pro-competitive approach is wavelength or fibre unbundling, as it would allow Communication Providers fuller control of the services they offer, versus being tied into what Openreach sees fit. This was highlighted by the European Commission in 2010 when it considered VULA to be a temporary solution. Vodafone has concerns that both FTTC and the FTTH fibre access architecture deployed by Openreach could effectively preclude such access or at the least necessitate costly future re-engineering, but sees nothing in the draft Plan indicating that Ofcom is planning to re-examine this issue.

5 : The Plan as a resource planning tool

Historic review of the Annual Plan shows that typically in the Draft Plan the areas of expected Ofcom activity are identified, and it is only when the Plan is finally published that dates are associated. While acknowledging the inherent uncertainties in scheduling much of Ofcom's activity, this massively reduces the worth of the draft version in the context of resource planning. Although industry stakeholders may represent large organisations, the level of skilled resource on regulatory issues is scarce, and it would be of great use if prospective timing for activities could be provided, for example in the form of a Gantt chart. Within this, we point to the resource drain presented not just by regulatory consultations, but also associated Information Requests and stakeholder engagement meetings.

6 : Detailed comments on the Plan

Ensure effective competition and investment in both current and superfast broadband (clauses 4.6 – 4.10)

Vodafone of course supports Ofcom's activity in this area. As highlighted above, we do consider VULA to be an important but ultimately interim solution and Ofcom's analysis should reflect this.

Vodafone continues to be frustrated by the discrepancies between the VULA requirements as laid down by Ofcom which were transposed into detailed technical standards by industry stakeholders via NICC Standards under the title of ALA, and Openreach's GEA service. Vodafone considers that a wires-only option should be made available for FTTC deployments immediately and, in the medium term, for FTTP too. We note that although the NICC standards set out QoS mechanisms for ALA, these have not been implemented by Openreach into their GEA solution. For stakeholders to make technical agreements, only to refuse to productise them downstream, devalues the currency of technical standardisation and will disincentivise participation in future industry engagement. We trust that these issues will be

considered by Ofcom in its analysis.

Implement the UHF strategy to enable a potential release of 700 MHz for harmonised mobile use (clauses 4.26 – 4.28)

There is no question that releasing further spectrum for public mobile unlocks far greater consumer surplus than any of the other uses to which spectrum may be put.¹⁴ Therefore, with the continued rise in mobile data demand, Ofcom must continue to work on the clearance and release of this spectrum for the benefit of the wider UK economy.

Following Ofcom's success in accelerating the clearance of 800 MHz spectrum, there is greater urgency than one might naturally expect to prepare for the release of the 700 MHz band. Given the need for harmonisation to maximise economies of scale in global equipment markets, we believe a detailed European band plan for the 700 MHz band needs to be finalised in time for the World Radio Congress in 2015. There are already competing proposals between using part of the Asia Pacific band plan (which Vodafone favours) and African / Middle Eastern plans where release of the Second Digital Dividend is likely to occur ahead of Europe. Ofcom can and should play a leading role in influencing this plan through its work in the RSPP.

Implement reform of non-geographic numbering to ensure price transparency (clauses 4.39 – 4.42)

Vodafone continues to support Ofcom's activity in this area. However, its proposals in other areas, most notably in relation to General Condition 9, will need to be implemented sensibly to ensure that they do not undermine this work. A proportionate approach to implementation and deadlines will also be required to provide industry stakeholders and our customers adequate time to make preparations for implementation.

Protect consumers in a range of priority areas, including silent calls (clause 4.43)

Vodafone understands the frustration experienced by customers who are plagued by silent calls, in particular those which are flagged as "CLI Unavailable" on landlines. We will therefore co-operate enthusiastically with Ofcom's activity in this area, whether by engagement in to-be-established groups examining process issues, or via our involvement in NICC Standards to address technical issues. However, we would caution that any network changes necessary to trace calls must be proportionate. Further Communication Providers can only provide pointers as to the source of such nuisance calls (and even this is in limited circumstances): unless this is backed up by firm regulatory and legal action against miscreant callers, or in the case of off-shore

¹⁴ Impact of Radio Spectrum on the UK economy and factors influencing future spectrum demand November 2012 <http://www.culture.gov.uk/publications/9498.aspx>

centres against the UK businesses which employ them, the exercise will be fruitless.

Review framework for regulatory financial reporting in telecommunications (clauses 5.5 – 5.6)

Vodafone welcomes Ofcom's commitment to improving BT's regulatory accounting output. The current regime is no longer fit for purpose with BT able to amend its regulatory financial statements to suit its own commercial ends. Ofcom needs to take steps to restore trust in BT's regulatory accounting output, ensuring that it is both robust and without bias.

Contribute to the consistency of communications regulation in Europe through BEREC and ERGP (clauses 5.7 – 5.9)

Vodafone welcomes Ofcom's participation at BEREC and ERGP and will provide support wherever that is useful. We consider that perhaps there is a missing communication/liaison channel in this area: it would be beneficial for both Ofcom and UK industry stakeholders if there was a mechanism by which industry could be kept abreast of the "hot topics" at European regulatory fora, and where appropriate provide industry feedback to inform Ofcom's position. It may be appropriate that Ofcom set up a co-ordination committee for this purpose.

Develop a forward-looking spectrum work programme (clauses 5.17 – 5.26)

Vodafone fully supports this activity. It would be of great use if Ofcom could publish, perhaps on the website, an holistic view of Ofcom's intended regulatory activity for each band on e.g. a three year timeline. This would greatly assist in resource planning.

Vodafone has been a strong advocate of Ofcom's efforts to provide greater regulatory certainty around E-Band licensing. Given the important role this spectrum will play in providing 4G backhaul, the acceleration of this work is now vital. We would urge Ofcom to get these regulatory rules in place as soon as possible and, in any event, no later than Q2 of 2013/14.

Addressing the needs of business consumers (clauses 6.8 – 6.13)

Vodafone notes that BT's service levels for the installation and repair of wholesale services is being considered within the WLA market review. However, we consider that service levels will need Ofcom oversight above and beyond the periodic market review and warrant a specific on going focus within Ofcom's work plan.

Technology is moving on at an unprecedented pace. However business customers' capability to adopt the newest most efficient solutions is hindered by the complexity of migration between legacy and more modern solutions. Within the BCMR we have called for an extension of the Network Access obligations to include this form of migration. We doubt that, without robust regulatory rules on migration, the commercial

incentives upon BT will result in the best outcome for end users (in particular for the complex migrations of business users). To set such rules we believe that Ofcom should, within the next 6 to 12 months, undertake engage with industry stakeholders, undertake further analysis and report back specifically on BT's capabilities and customer requirements for migration. Ofcom should then publish 'best practice' guidance on the key migration requirements, enforcing these by dispute resolution or ex-ante rules if necessary. Vodafone would be very happy to take part in such a workstream.

It will be necessary to examine in detail the migration requirements of each market and we recognise that often BT lacks the appropriate incentives to provide a timely and appropriate solution. This is particularly marked where CPs and BT purchase varying inputs or are at different points in product take up or product life cycle.

For example in the context of Ethernet services we have been attempting to negotiate with BT without conclusive resolution for 3 years on process and commercial adaptations that would facilitate migration from legacy to modern Ethernet services. In the case of business customers, migration is dictated by individual customer requirements and the ability to have network down time or not and the extent of down time that is deemed acceptable. This is why in the context of Ethernet it is necessary to adopt migration solutions that have parallel running, hot cut over and out of hours hot cut over.

Vodafone Limited
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