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28th June 2016

To whom it may concern,

### **Designing a new broadband USO Obligation – call for inputs**

This letter is the response of Three (Hutchison 3GUK Ltd) to Ofcom's call for inputs on Designing a new broadband USO obligations. It complements responses made by Three to Government consultations on this same subject. It also follows on from a meeting Three had with Ofcom on the 9<sup>th</sup> of June where we set out what we consider to be the key issues that need to be considered.

Connectivity has rightly become an important political issue and it is appropriate for Ofcom to advise Government on regulatory interventions to extend fixed coverage in hard to reach areas, where it may never be possible to deliver connectivity effectively on a commercial basis. Three welcomes the opportunity to provide input into Ofcom's process, that we understand will conclude with a comprehensive report to government recommending how a universal services obligation [USO] for broadband services should be implemented.

The purpose of this letter is to summarise the concerns we discussed with Ofcom on 9<sup>th</sup> June. Separately we are considering technological methods that could be used to deliver a broadband USO, however this is in the early stages, and our initial thoughts are that potentially our limited network reach may make the commercial case of this challenging for us in any procurement process.

The three main issues we cover in this letter are; (a) the scope of the USO, (b) the funding of the USO, and (c) the competitive impact of the USO.

#### **(a) The scope of the USO**

The EU Universal Service Directive states that the USO is an obligation relating to fixed network operators, and not an obligation on all communication providers. [ 3< ]. Three is concerned for two reasons (i) We feel the broadband USO should be a fixed operator

obligation, and (ii) any further coverage obligations placed on us could seriously adversely affect our competitive position.

(i) A fixed operator obligation:

Three's view is that a broadband USO is, and should be an obligation on fixed operators. This service has traditionally been provided over the fixed network. Fixed operators extend their connectivity to areas where it is commercially economic to do so. Absent fixed connectivity in these harder to reach rural areas, connectivity will be incredibly challenging through other technologies.

(ii) Further coverage obligations on Three:

Three as the smallest mobile network operator is concerned that any USO may burden us disproportionately with significant additional costs through further coverage obligations.

[ X ]. In December 2014, the UK Government concluded a binding agreement with the four MNO's, for them to provide voice and text coverage to 90% of the UK's land mass by December 2017. [ X ].

In our response to Ofcom's Consultation on Additional spectrum licence Fees in April 2015 we explained the detail of some of these challenges.<sup>1</sup> Any further coverage obligations, although potentially costly for all operators will be particularly challenging for smaller operators because; firstly existing coverage is likely to be less when compared to larger operators, smaller operators have greater coverage to 'make up', and secondly because smaller operators have fewer potential customers in any given area and therefore network extension is likely to attract fewer customers, thus putting pressure on the commercial viability of such roll-out.

(b) Funding of the USO

BT as the dominate provider is currently subject to a USO; the burden this places on BT is periodically assessed by Ofcom. This assessment considers the revenues and benefits generated by the USO and the costs to provision the services under the USO. Three considers that the first test Ofcom should satisfy is to establish why, and indeed if this additional USO represents any further significant burden on BT. Given the scale of BT especially post the acquisition of EE, and their current network reach Three considers it is possible that extending BT's USO may, in context place very little incremental burden on them.

In the event that Ofcom considers that the additional USO is likely to place a significant burden on BT then, notwithstanding the competition issues discussed in part (c) below Three believes the government should provide the funding. There is very recent precedent for this in the case of the BDUK funding, where the government provided in the

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<sup>1</sup> Three's Response to Ofcom's Annual Licence Fee Provisional Decision and Further Consultation 17<sup>th</sup> April 2015

region of £2 billion to enable people in more rural and remote areas to receive superfast broadband services. This proposed new broadband USO is also for the provision of broadband services in remote and rural areas, thus logic underpinning the case for the government to provide funding appears to be strong – although steps would have to be taken to ensure that this model did not further distort competition within the market – considered below

If neither of these options is considered feasible by Ofcom, then we consider the only remaining option is for fixed operators to provide the funding, in line with the Universal Service Directive that this obligation falls on fixed operators. In this event, consideration should be given not only to the simple methods of allocating this burden between fixed operators based on revenue, but also methods such as allocating the burden based on the current value of an operators fixed network. Using these types of burden allocation methods could positively influence competition by placing a higher burden on operators that have the most advantage in terms of network reach.

### **(c) Competitive impact of the USO**

Operators with the largest network reach have a natural competitive advantage. Costs within the telecoms industry are largely fixed, thus there are significant economies of scale advantages that can be achieved with large networks and large numbers of customers. In the UK we now have one dominate provider for both fixed and mobile services that dwarfs all the other operators with combined revenues in the region of £25 billion, the next largest operator being SKY with revenues a little higher than £7 billion.

The upmost consideration must be given to the effects this USO may have on the competitive landscape of the UK telecoms market. The USO will affect few people in the remote rural areas of the UK, whereas a distortion of competition in the UK telecoms market could potentially affect everybody in the UK.

If funding is to be awarded through some kind of procurement process it is vital that the following considerations are taken into account:

- 1) The procurement process should not simply consider cost, in the event that it does the likely winner in every case, due to their ubiquitous network that already exists is BT/EE.
- 2) The procurement process should consider geographic regions and allow bidding in each area, thus enabling greater competition and a large number of potential bidders.
- 3) If an operator's network is extended through funding being provided to them, then other operators should be able to access this network in order to also be able to provide services on fair and reasonable terms and importantly costs.
- 4) The greater the number of different operators that provide this USO the more positive the influence on competition in the market.

## Conclusion

Three considers that Ofcom must first give careful consideration to whether any intervention over and above the current USO is justified, and indeed whether the current USO could simply be extended.

In the event that this is not possible Three considers that careful consideration must be given to the design of the USO, because although it may improve broadband coverage in a small part of the country, it has the potential to distort competition in the whole of the country. Any operator that receives funding to extend their network reach gains a competitive advantage. However as discussed in this response there are ways to negate the effects of this competitive advantage.

We are very keen to maintain engagement with Ofcom and share our thoughts as they develop over the coming months.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Leanne Bruce', with a long horizontal flourish extending to the right.

Leanne Bruce  
Regulatory Analyst