

INCA response to Ofcom consultation on price regulation In Area 3

INCA is pleased to respond to Ofcom’s consultation on price regulation in Area 3 (the Area 3 consultation), which forms part of the wholesale fixed telecoms market review (WFTMR). The Area 3 consultation presents a change to the proposals set out in the WFTMR consultation, issued by Ofcom in January 2020.

Instead of the post-build RAB approach set out in the WFTMR, Ofcom is now proposing a forecast RAB approach (the forecast approach). This is in response to BT offering a commitment to deploy fibre networks to 3.2m premises in Area 3 (the BT Commitment).

Introducing INCA

INCA is the association of the UK’s independent network operators – full fibre and wireless, suppliers to the sector, local authorities, consultants, and professional services organisations.

- INCA supports the development of sustainable independent networks through collaboration on the provision and procurement of products and services and adoption of common standards.
- INCA supports collaboration between members to create new, independent digital infrastructure that can be shared by operators and suppliers.
- INCA supports mutual trading between members.
- INCA represents the interests of independent networks to government and regulator
- INCA promotes the advantages and successes of independent networks.

Ofcom's Area 3 definition

In order to comment on Ofcom’s proposed price regulation for Area 3, it is necessary to consider where and to what types of locations that regulation would apply. In the WFTMR, Ofcom’s proposed definition for Area 3 was:

“a geographic market comprising postcode sectors where there is unlikely to be material commercial deployment by rival networks to BT”

Ofcom originally proposed to define geographic markets using transparent and consistent parameters to determine where commercial deployment would be viable. This approach was however abandoned, in favour of using operator’s existing coverage and build plans. It is disconcerting, however, that Ofcom only included coverage and build plans for the very largest altnets, not even including existing coverage from other altnets.

In V2 paras 7.20-21 of the WFTMR, Ofcom stated as follows:

“In this analysis we have considered the current and planned rollouts of Virgin Media, CityFibre and FibreNation. These networks have existing coverage; have been able to provide us with rollout plans; and either already provide both WLA and leased lines or have identified that their business plans assume the provision of both services.

7.21 Other networks may start rolling out prior to our final statement (for example, Axione²²⁹). In addition, some networks that we have considered to be broadband only networks may be able to provide leased lines if demand arises. If such developments were to occur, we would need to consider updating the MSNs included in our analysis for our statement. “

Many other altnets also had existing coverage, however, as well as business plans and they identified in those plans that they would provide both WLA and leased lines services. Ofcom offered no explanation (then or now) for why such existing coverage and plans were ignored.

Many of BT’s rival networks are INCA members and many have submitted existing and planned fibre coverage data to Ofcom¹, our analysis shows, however, that existing and planned deployment by several INCA members have nevertheless been categorised as Area 3. INCA is also aware that some locations on building plans submitted by the larger altnets included in Ofcom’s analyses have been categorised as Area 3. Again, we are not aware of any transparent rationale for this inconsistency.

Despite several attempts to receive clarification from Ofcom as to why this was the case - for example, was it linked to Ofcom’s definition of what constitutes material commercial deployment – neither INCA nor INCA’s advisors or individual INCA members have received such clarification.

In conversations Ofcom has referred to the complexity of processing the plans for many small operators and the uncertainty Ofcom assigns to such plans (compared to BT’s plans and the plans of the largest altnets - CityFibre, FibreNation, and Virgin media – from which Ofcom has accepted plans submitted and has categorised locations in those plans as Area 2), but nothing more precise has been received in respect of Ofcom’s definition of material commercial deployment and why the plans for many altnets (some with plans to deploy fibre to >1m premises in the relevant period 2021 – 2026) have been categorised as Area 3.

INCA is deeply concerned at this lack of transparency on Ofcom’s approach. We understand that Ofcom has discretion in its analyses and decision-making, but, overall, it should ensure that such analyses are transparent and consistent.

¹ Although it should be noted that a significant proportion of INCA members did not receive s.135 data requests in order for Ofcom to include their data in its WFTMR analyses.

Further, Section 135 requests to altnets, requesting data on existing coverage and build plans, are presented as critical input to Ofcom for final decision-making on the scope of WFTMR geographic markets. Given the substantial amount of feedback Ofcom has received from altnets, INCA hopes Ofcom will revise its approach to geographic market definition and include existing coverage and build plans for all altnets.

INCA commissioned Point topic to assess the current FTTP deployment in Area 3 and below we present the results: The table below relates to FTTP actual deployments reported at Q3 2020, showing premises passed by Openreach and altnets.

FTTP deployments in Area 3	# premises passed
Openreach only areas	609,978
Openreach/altnet wireless areas	45,087
Openreach/altnet FTTP areas	10,832
Altnet-only areas	392,521
Total	1,058,418

It can be seen that altnets have already deployed to over 400k premises in Area 3, and Openreach to almost 666k, giving a combined FTTP in Area 3 total of over 1m premises. Incan considers that this, at the minimum, means that Area 3 should be redefined to exclude those premises.

Additionally, the table above shows that overlap areas, where FTTP networks have been deployed by both Openreach and altnets are less than 11k premises (around 1% of total), which supports our view that operators will avoid overbuilding, and will choose to deploy in areas which are unserved by FTTP. This approach is consistent with many parts of Area 3 being able to support only a single network and it shows that both Openreach and altnets are making very material deployments in Area 3, contrary to Ofcom's assertions that altnet deployments in Area 3 are not material.

As evidenced by the build plans submitted to Ofcom by altnets, many locations currently classified as Area 3 are attractive for commercial deployment and thus very clearly cannot be characterised as locations "*where there is unlikely to be material commercial deployment by rival networks to BT*". On the contrary, they are locations where altnets have firm plans to deploy, often substantially in advance to BT and thus offering real economic benefits to those locations.

Whilst the forecast approach to price regulation in Area 3 results in the same price regulation and thus the same price levels, in Areas 2 and 3, there is still a significant impact

of the Area 3 interpretation by Ofcom, namely that the BT Commitment can consist of locations already being target deployment areas for altnets.

In discussions with Ofcom it has become apparent that the continued altnet concern with the Area 3 definition has come as a surprise to Ofcom. We understand that Ofcom's expectation was that, with the price regulation being the same as in Area 2, the boundary between Areas 2 and 3 would no longer be of significant concern to altnets. This is clearly not the case and INCA's WFTMR response stated clearly that a pre-commitment by BT would distort the fair market competition that does exist in places, and reduce the likelihood of altnets deploying in these locations at all, and even worse, overbuild of an altnet's existing operations in Area 3 when two full-fibre networks are not sustainable. Below is an extract from INCA's WFTMR response:²

- 1. If Openreach makes binding commitments to invest in Area 3, the downward pressure on the 40/10 FTTC pricing will be alleviated or perhaps removed. It would, however result in Openreach deploying full-fibre in all the most commercially attractive parts of Area 3, significantly increasing the risk that altnets would be overbuilt in areas where it is unlikely that two full-fibre networks are sustainable.*
- 2. Openreach has a significant existing customer base to migrate across to its fibre network (including its downstream retail ISPs that form part of BT group and large retail ISPs that currently use the Openreach FTTC wholesale services). That means that overbuild by Openreach would increase the risk for altnets deploying in Area 3 substantially. The forecast approach may in fact prove higher risk to altnets than the RAB approach.*
- 3. As INCA is aware of plans by altnets to deploy full fibre to around 4m premises in Area 3, we do not believe that Openreach investment under the forecast approach would deliver superior economic benefits to that.*

Given the level of concern expressed in our WFTMR response with regards to the forecast approach, INCA is concerned that Ofcom should be surprised at the widespread concern and critique of the BT Commitment. INCA is aware that the same concern was expressed in responses by some of its members, further adding to our confusion as to how Ofcom could have not been aware.

² Paragraphs 133 – 135 of the INCA WFTMR response

The forecast approach

INCA supports the application of the CPI-0 charge control in Area 3. This is because our members have substantial plans to deploy fibre in locations currently classified as Area 3 and therefore it is right to include investment incentives for all providers, not just for BT (as was the case in the post-build RAB approach). This situation arises because Ofcom has misclassified locations into Area 3, which should rightly be in Area 2.

INCA has some difficulty supporting Ofcom's forecast approach, however, as it combines the CPI-0 charge control with the BT Commitment. The BT Commitment effectively translates into the opportunity for BT to select locations, publish its intentions and effectively sit back and deploy to those locations whenever it fits with BT's own plans – with near certainty that no one else will deploy there due to the impact of the BT statements of commitment to Ofcom.

Although the BT Commitment is not a formal obligation, it is our view that it will be considered by local authorities, retail providers and large customers as a contract between BT and Ofcom that provides certainty that BT will deploy in the relevant locations. We have informal information from altnets that local authorities have already reacted to the BT Commitment announcement by discontinuing discussion with altnets.

INCA understands that, in locations where there are no commercial incentives for altnets and/or BT to deploy fibre, it would be prudent for Ofcom to require a 'quid pro quo' commitment from BT to invest in return for higher prices for the 40/10 anchor wholesale access product. However, given that at least 4m of the just under 9m³ premises currently categorised as Area 3 are already targets for commercial deployment by altnets, it is difficult to understand why a compensating commitment from BT is required for those locations.

If Area 3 genuinely comprised of locations where it is uneconomical to deploy commercially, then a compensating commitment would be appropriate, but it would also be commensurately smaller as it would only have to compensate for higher prices in the areas where no commercial deployment would take place. The combination of a smaller number of premises being genuinely uneconomical and a higher cost per premise to deploy fibre would likely result in a requirement for a BT Commitment for between 1m and 1.5m premises. Ofcom's interventions should also take into account known Government initiatives to reach the final 20% of premises in the country (the F20). Given that the F20 initiative covers approximately 5m premises and there are altnet plans to deploy to around 4m premises, then it seems that all of Area 3 is already potentially covered (being a total of 8.8m premises) and there is in reality no need for any special compensating commitment from BT in return for the CPI-0 charge control.

³ 8.8m

The CPI-0 charge control will simply ensure that there is sufficient headroom in the Openreach wholesale charges to incentivise both BT and altnets to invest and the F20 initiative will cover the remainder of the Area 3 locations. If instead copper prices were reduced in locations where altnets have built or are currently planning on building in Area 3, such reductions, would have a negative impact on take-up of Fibre products and delay copper-switch off in an area.

In addition to the considerable harm the BT Commitment would cause to altnet investment and deployment prospects, the BT Commitment would likely result in a lower overall fibre deployment in Area 3. This is because the BT Commitment covers premises that would have been covered commercially in any case, but the impact of the BT Commitment would likely be such as to harm altnet financing overall due to lack of confidence in the market resulting from increased regulatory risk.

The need for impact assessment

INCA is concerned that the Area 3 consultation does not include an impact assessment. We have considered whether the impact assessment in the WFTMR could be considered to cover this associated consultation, but have concluded that this could not reasonably be considered to be the case, given that the forecast approach is in no way detailed in the WFTMR. It would simply have been impossible to cover that regulatory proposal that is mentioned in passing in only 3 paragraphs⁴.

As is evident from the analysis set out above and the responses submitted by individual INCA members, there are significant market impact resulting from the BT Commitment, resulting, we believe, in reduced fibre deployment in Area 3 and consequently consumer harm relative to the counterfactual where no BT Commitment was imposed. INCA is concerned that absent a full impact assessment, the Area 3 consultation is not in compliance with Ofcom's formal duties⁵.

Ofcom's proposals do not maximise consumer benefits

As set out above, it is our strongly held view that Ofcom's proposals (in particular the BT Commitment) will result in delayed and reduced fibre deployment in Area 3. This is because altnet deployment prospects will be weakened by the BT Commitment and BT will be under substantially less competitive pressure to deploy quickly in Area 3, as there will be much reduced probability of altnet deployment ahead of BT.

⁴ WFTMR V4 paras 2.27-29.

⁵ Communications Act 2003 section 7.

INCA notes that Ofcom has a formal duty to maximise consumer benefits⁶ and as such we consider that the Area 3 consultation proposals are not in compliance with that duty.

Proposals for change

Remove commercially viable locations from Area 3

The core of the issues identified by INCA, its members and other altnets, is that Ofcom has miscategorised a large number of premises as Area 3, when they should be Area 2.

Therefore, the most appropriate means of overcoming that issues would be to reallocate locations where altnets have planned deployment from Area 3 to Area 2.

Whether Ofcom then considered it necessary for BT to make a commitment to compensate for the CPI-0 charge control in the remainder of Area 3 would depend on the extent to which Ofcom believes the F20 initiative will deliver connectivity to the remainder of the premises in Area 3. Given, however, that the Area 3 locations would be those that are genuinely uneconomical for commercial deployment, it may not be appropriate to expect BT to deploy there without state aid and, Ofcom incentives across the F20 initiative locations could cause more harm than benefit.

INCA therefore recommends that Ofcom remove locations from Area 3 for which altnets have submitted deployment plans⁷. Once that has been done, Area 3 should be almost identical to the F20 scope and thus should be addressed through that initiative.

Should some locations fall into the gap between commercial deployment and state aid deployment, that is likely to be a small number of locations and such locations could be addressed in the next market review if they remain unconnected to fibre.

Restrict the locations available to BT for its commitment

Should Ofcom decide to not reallocate commercially viable locations to Area 2 (a decision which INCA considers may be subject to legal challenge), then Ofcom should create restrictions on which locations BT could include in its commitment.

A simple rule would be that BT cannot include in its Area 3 commitment any locations that have been included in an altnet build plan submitted to Ofcom. The logistics and practical

⁶ Communications Act 2003 section 4(8) (b).

⁷ It should be noted that INCA remains of the strong view that using deployment plans to define Area 3 is inferior to the application of consistent and transparent criteria for defining where commercial deployment is viable.

implementation of such an arrangement would need to respect the commercial confidence of individual altnet deployment plans but could be done at the aggregate level.

The BT Commitment should also not include locations where BT has already deployed fibre at the time of the introduction of the new charge control in April 2021. The inclusion of locations where BT has already made commercial decisions to roll out fibre is indirect conflict with the need for commitment in the first place. The fact that BT has already deployed fibre to app. 0.5m premises in Area 3 and will potentially have deployed to close to 1m premises by the start of charge control testifies to the fact that Ofcom has miscategorised locations as Area 3, when they should be Area 2. Locations that are commercially attractive for BT to deploy to are also commercially attractive for altnets to deploy to and would have been covered by altnet networks, had BT not started first.

The purpose of the BT Commitment is to ensure that as many consumers in Area 3 as possible benefit for fibre connectivity. The advance coverage of significant parts of Area 3 by BT and altnets is clear evidence that such locations should not be included in Area 3.

[Adjust the BT Commitment dynamically to reflect actual altnet deployments](#)

In any circumstance where a BT Commitment is in place, Ofcom should ensure that this is communicated as a representative sample of locations to be covered by BT, which will be adjusted if an altnet either completed deployment in a specific location or communicates to Ofcom that it has committed funds for the build and has notified the Highways Authority of its build plans.

Such an arrangement could, to an extent, soften the impact of the BT Commitment on the market. With the right communications from Ofcom it should be possible for altnets to negotiate with local authorities and national retail operators to enable deployment in locations on the BT Commitment list.

It would, however, be important that any such arrangement would be sufficiently granular to enable the removal of locations from BT's list at the village size scale (between 200 and 500 premises, typically), if not then that would deter commercial altnet deployment in those harder to reach locations, and likely delay availability of fibre in those locations.

In order to be effective, the revision of the BT Commitment list and the communications of that should be a public process and should happen every 2 months.

Ofcom's proposals remain discriminatory against altnets

In our WFTMR response we presented why Ofcom's proposals for Area 2 are in direct conflict with Ofcom's formal duties to not discriminate for or against different (or different types of) communications providers.

By allowing BT to select its commitment areas Ofcom is giving BT clear preference to deploy to those areas. This is despite Ofcom having received deployment plans for altnets that cover many of those areas. This will without doubt prove harmful to altnet deployment abilities even beyond the scope of the BT Commitment.

Ofcom has formal duties not to discriminate for or against individual or types of communications providers. The relevant provisions are set out below.

Communications Act 2003 4. (6)

- The fourth Community requirement is a requirement to take account of the desirability of OFCOM's carrying out their functions in a manner which, so far as practicable, does not favour—
 - (a) one form of electronic communications network, electronic communications service or associated facility or
 - (b) one means of providing or making available such a network, service or facility, over another. [emphasis added]

and

The European Electronic Communications Code 3. 4. (b)

- ensure that, in similar circumstances, there is no discrimination in the treatment of providers of electronic communications networks and services;⁸ [emphasis added]

It is INCA's view that the clear preference of BT deployment over altnet deployment may be open to legal challenge, should Ofcom decide to proceed with it.

If Ofcom feels there is a need for a commitment to cover large parts of Area 3, then it should make the opportunity of making that commitment available to all operators. INCA is certain that several altnets would welcome the opportunity to make such commitments in return for public statement that they have entered into such arrangements with Ofcom.

No such opportunities have, however, been extended to altnets. Whilst we understand that Ofcom regulated only BT as the operator found to have SMP in the relevant markets, the

⁸ Note that the EECC is expected to be in force when Ofcom issues its Final Statement on the WFTMR.

commitment(s) could be sourced from a number of operators and have a much more positive effect on the market.

Pricing of wholesale leased lines and dark fibre in Area 3

In the WFTMR Ofcom acknowledges that in order to encourage investment in new fibre infrastructure, it is necessary to regulate consistently in broadband and leased lines markets. This is because the two markets are served by the same upstream infrastructure and without access to the economies of scale and scope enjoyed by BT, altnets cannot make positive investment cases to attract funding.

Ofcom has imposed the CPI-0 charge control on the BCM in both Areas 2 and 3 but has decided to impose a dark fibre remedy in Area 3.

Regulating adjacent upstream markets can result in conflicting investment signals unless the pricing approach is consistent across all levels. This is best known as the investment ladder principle, in which there should be economic space between each step ladder in order that there is an incentive for a competing provider to 'climb the ladder' through investment in competing technologies, fibre and perhaps even passive infrastructure.

This means that it should be possible for a provider on a higher level of the ladder to replicate the downstream products offered by the incumbent, thus an investor in fibre (using PIA) should be able to replicate the regulated wholesale dark fibre price.

Ofcom has, however, proposed to set the pricing for dark fibre in Area 3 at a level that is not replicable. This means that the altnet using PIA would not be able to compete with BT on providing dark fibre to service providers serving the point-to-point market, as those service providers can buy regulated dark fibre from BT at a price that is not replicable by the altnet.

The altnet is thereby denied access to the economies of scope and scale available to BT and thus Ofcom is internally inconsistent in the application of its own stated approach and underlying platform for encouraging increased and accelerated fibre deployment across the UK. Given the nature of Area 3 (being more rural with longer distances between premises and thus higher cost to serve each premise), all economies of scale and scope are of critical importance and INCA urges Ofcom to revise its position on dark fibre pricing.

As Ofcom is now proposing consistent charge controls across Area 2 and 3, what is the justification for the continuation of the dark fibre costing approach? INCA can understand why a dark fibre product could be of value in Area 3, but it should not be provided at the cost of harming the investment case for altnets.

Discounts and contractual pricing incentives

Ofcom proposes in the Area 3 consultation to extend its proposed restrictions on geographic discounts to Area 3. The restriction was initially proposed only for Area 2.

INCA strongly welcomes this proposal as this will certainly reduce the perceived risk of BT taking local pricing action to harm local altnet deployment initiatives. INCA also welcomes this as an indication that Ofcom has come to appreciate the amount of commercial deployment altnets are planning for Area 3, and the value of that deployment.

INCA is, however, disappointed that Ofcom has not chosen to also extend its proposed restrictions on other forms of potentially anticompetitive pricing behaviour. If Ofcom recognises the value of altnet deployment in Area 3 then it must also recognise the threats to that deployment by potential BT pricing behaviour including loyalty arrangements, volume discounts and other similarly disruptive pricing initiatives which Ofcom proposes to leave unrestricted in Area 3. Once Again it seems that Ofcom's approach is internally inconsistent, giving rise to increased uncertainty and risk.

In addition to extending restrictions on potentially anticompetitive pricing initiatives to Area 3, INCA refers Ofcom to our WFTMR response, in which we present our analysis of why we believe that Ofcom's proposals do not go far enough and still leave scope to BT to do real harm to altnet investment prospects.