



Business Connectivity Market Review
Preliminary Consultation on Passive Remedies

Response to the Consultation
Submitted by: CityFibre Holdings Limited

5th January 2015

CityFibre's Response to the Preliminary Consultation on Passive Remedies

Published 5th November 2014

I. Introduction

1. CityFibre welcomes this opportunity to respond to the consultation document titled Business Connectivity Market Review – Preliminary Consultation on passive Remedies, published by Ofcom on 5th November 2014 ("Consultation").
2. CityFibre is an operator of all-fibre networks in major UK towns and cities. We design, build, operate and own passive fibre infrastructure that is deployed on a city-wide basis. Our networks are used by ISPs, integrators and MNOs ("CPs") in a shared infrastructure wholesale model, providing fibre optic connectivity to public services, cell-sites, businesses and homes.
3. CityFibre is the UK's largest independent provider of fibre infrastructure with networks deployed in 60 towns and cities. We are leading the rollout of Gigabit Cities throughout the UK, with projects deploying city-wide FTTP infrastructure now underway in York, Peterborough, Coventry, Aberdeen, Huddersfield and Hull.
4. CityFibre is a member of a joint venture with Sky and TalkTalk bringing Gigabit FTTH to residents in the City of York utilising a pure fibre network that is independent of BT Openreach. The parties have announced their intention to expand the venture to a further two cities. Furthermore, CityFibre owns one of the UK's largest current FTTH networks in Bournemouth.
5. In January 2014 CityFibre listed on the AiM market of the London Stock Exchange. We are supported by top tier institutional investors, providing capital to deliver Gigabit City projects in up to 25 cities. Furthermore, CityFibre is pre-qualified for infrastructure debt guarantees from HM Treasury's UK Guarantees Scheme administered by Infrastructure UK.
6. CityFibre's response to this consultation is divided in to three parts. Part II provides context to our submission Part III includes CityFibre's response to the questions posed in the Consultation. No claim for confidentiality or business secrets is being made in respect of this submission.

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II. Context for CityFibre's Comments

1. **Preliminary comments.** We note that this Consultation is a preliminary consultation on the subject of passive remedies and a further step in the consultation process is expected in Spring 2015. As CityFibre is still analysing the impact of passive remedies on CityFibre's business, we have restricted our comments in this response to a small number of high-level points. If appropriate, we will expand on our arguments in the later stages of the consultation process.
2. **CityFibre is not a CP.** The comments that CityFibre makes in this submission are in respect of our role as a builder of passive infrastructure. CityFibre prefers not to provide services to end users in the downstream markets.
3. **CityFibre does not use BT infrastructure.** In the context to this Consultation our comments are not directed to our desire to access BT infrastructure, but are related to our build of passive infrastructure as a competitive alternative to BT.
4. **CityFibre is a passive infrastructure builder.** We build passive infrastructure and operate a wholesale model providing dark fibre products to fixed and mobile CPs in Business Connectivity and NGA markets. We believe it is essential for the UK's digital infrastructure to be modernised towards pure fibre and wireless technologies. To achieve this, new passive infrastructure must be built with reduced dependency on BT and with minimal State intervention.
5. **New passive infrastructure must be:**
 - **Fit-For-Purpose.** Communication is now digital and rapidly becoming ultrafast, so the infrastructure underpinning digital communications must be built specifically for this purpose. We believe that legacy copper and cable networks should be retired in the mid-term, being replaced with newly built fibre networks with sufficient dark fibre to future-proof any scenario of data growth.
 - **Shared Infrastructure.** We believe that passive infrastructures should be shared, supporting all segments of the market. CityFibre's approach delivers passive infrastructure via dark fibre to CPs in all market verticals, enabling them to shift towards consuming infrastructure rather than consuming bandwidth.
6. **Gigabit Cities.** CityFibre is deploying fit-for-purpose, shared passive infrastructures in towns and cities across the UK, supported by fixed and mobile CPs. Our dark fibre networks provide unrestricted bandwidth and are deployed with substantial fibre capacity for all future connectivity needs. Our Gigabit Cities provide a template for digital infrastructure that is applicable and replicable nationwide.
7. **Embracing the new generation of fibre infrastructure builders.** BT is unable to undertake the modernisation of digital infrastructure alone – recent history has demonstrated BT's dependency on significant state assistance. BT's ability to invest in content, push into mobile services, fund dividends and pension obligations will limit its appetite to invest in infrastructure. For the UK to transition to the infrastructure needed to remain globally competitive, regulators and Government must embrace the new generation of fibre infrastructure builders.
8. **Infrastructure competition is essential.** A regulatory and policy environment that proactively encourages true infrastructure competition aids investment by CityFibre in new passive infrastructure.
9. **Passive remedies may introduce risks to infrastructure competition.** The mandated introduction of passive remedies requiring BT to offer dark fibre products to CPs changes the competitive environment and may introduce risks and uncertainty that undermines CityFibre's investment. Our preliminary comments in this response address these concerns.

Part III

Comments and Observations on the Consultation

Our comments to the Consultation are provided below. For ease of reading, the questions posed in the Consultation are included in *green italicised text*, followed by CityFibre's response.

As the Consultation is at the preliminary stages, we have limited our comments to a small number of salient points that we feel are important to raise at this stage. We welcome engagement with Ofcom during the process to further our arguments as the Consultation progresses.

Question 1: Do you agree with our preliminary framework for considering the case for passive remedies?

1.1 Ofcom must support and encourage infrastructure competition

In accordance with the EU regulatory framework that promotes competition at all levels of the communications market, we believe that Ofcom has a duty to enable and ensure a competitive supply of communications infrastructure where possible.

When looking at the current state of the UK communications market, the competition problem is predominately at an infrastructure level. Historical focus on service competition has resulted in a vibrant CP market with many service providers operating today. However, most CPs are dependent on the use of BT's infrastructure resulting in the significant competition problems identified by Ofcom coupled with the large extent of BT's SMP and the regulatory remedies enforced by Ofcom.

Passive remedies imposed on BT do not address the fundamental issue of infrastructure competition, and if introduced may have the effect of further strengthening BT's already dominant position with negative outcomes for the industry longer term.

Ofcom's primary considerations must be directed to supporting real competition at an infrastructure level, ensuring that any review or introduction of passive remedies does not undermine this objective.

Passive remedies may undermine the desire or ability for CityFibre (and other firms) to invest in building new passive infrastructure if:

- Passive remedies are introduced too soon;
- Pricing of passive remedies undermines the case for investment in alternative infrastructures;
- Conditions attached to passive remedies are poorly considered and/or poorly implemented.

1.2 Passive remedies may stifle infrastructure competition

Paragraph 2.24 of the Consultation states *"If passive access provides a lower-cost or lower risk route to market than self build, this would change the future returns on past self build decisions and reduce the incentive for self build in areas where CP's (other than BT) are not yet present."* In other words, the introduction of passive remedies may slow or stop investment in alternative infrastructures thereby increasing dependency on BT.

Time is needed for infrastructure competition to become established in the UK, especially in local access and backhaul segments. As new infrastructure build is both capital intensive and time consuming, the introduction of passive remedies that result in BT introducing dark fibre products should not occur until the supply of alternative

passive infrastructure is well established.

Therefore, as the introduction of passive remedies may reduce the incentives for infrastructure competition, CityFibre does not support the introduction of passive remedies in the 2016-2019 period.

1.3 CPs unlikely to self build, but they seek alternatives to BT

As Ofcom points out, a number of CPs have constructed some infrastructure (Vodafone, Level 3, Verizon, EU Networks, Colt and Virgin are examples). With the exception of Virgin Media, these past investments were focused in national long-haul networks or business connectivity infrastructure in the London WECLA areas.

CityFibre's experience, from four years of extensive dialogue with the industry, indicates that the majority of CP's are unlikely to 'self build' alternative networks solely for their own use – due to unviable economics and unnecessary asset duplication. For many CP's owning and operating infrastructure is not core to their business models. However, all CPs that we have engaged with share a strong desire to consume infrastructure from an alternative supplier to BT.

CPs share many common themes when considering the supply of infrastructure:

- **Supply from a neutral party** – that is not competing with CPs in the downstream retail markets;
- **Availability of passive products** – predominately dark fibre;
- **Infrastructure tailored to their business** – enabling innovation in network architectures and service development;
- **Improved service levels** – than currently available from BT.

Whilst the framework considered by Ofcom in the Consultation addresses some of the above points, it does not address the desire of CPs for an alternative infrastructure supplier to BT.

1.4 BT's increasing market dominance

Potential industry consolidation and evolution to quad-play has potential to significantly increase BT's market dominance in the short to medium term. BT's stated plans and actions to move into both mobile (e.g. the announced intent to acquire EE) and content (e.g. BT Sport) demonstrates this.

Furthermore, such market changes are likely to distract BT away from infrastructure upgrade and deployment beyond current BDUK commitments in the short term – a period when investment in fibre infrastructure is critical for the overall wellbeing of the UK digital infrastructure.

When considering the availability and supply of fibre infrastructure to CPs, Ofcom should be careful not to implement measures that 1) further aids BT's dominance and 2) have an undesired effect of undermining investment in alternative fibre infrastructures.

1.5 The role of CityFibre in the UK infrastructure market

CityFibre is investing in the deployment of new passive infrastructure in UK towns and cities outside of the London WECLA areas. We are creating the UK's first scalable open access passive infrastructure company in the local access market – providing end-to-end dark fibre products that are consumed by CPs.

Our networks provide business connectivity and backhaul connectivity (point to point dark fibre) and are expandable to NGA connectivity (typical PON based FTTP/FTTH)

as is currently being deployed in York in conjunction with our JV relationship with Sky and TalkTalk.

CityFibre addresses the key infrastructure needs of CPs as outlined in 1.3 above – a neutral supplier of passive infrastructure aligned to the business models of our customers. Furthermore, with no legacy issues such as pension obligations, maintaining copper networks etc., we are an ‘efficient investment vehicle’ ensuring that new, fit-for-purpose infrastructure is deployed effectively in a shared infrastructure model.

We feel strongly that CityFibre is playing an essential role in addressing the infrastructure competition issues in the UK market. As the primary independent ‘NetCo’ we believe that Ofcom has a duty to establish an environment for our business to develop and thrive. Passive remedies may impede CityFibre’s progress.

1.6 Efficient Asset Duplication

As stated in 1.3 above we believe that CP ‘self build’ is not economically attractive and unlikely to occur in scale. This points to the need for shared infrastructure models.

CityFibre’s shared infrastructure model promotes the new build of ‘fit-for purpose’ passive infrastructure. The reason for this approach is that new build delivers fibre infrastructure in a passive architecture with capacity that is better suited to modern ultrafast communications. In contrast, incremental upgrades to legacy copper routed networks is operationally challenging and inefficient.

CityFibre’s overbuilding of BT’s infrastructure will lead to some duplication of assets. We believe this is necessary for the UK’s digital infrastructure to be modernised effectively. We refer to this overbuild as “Efficient Asset Duplication” whereby our new fibre infrastructures are open and shared, providing passive dark fibre to CPs with flexibility for them to architect their own networks and services.

We raise this viewpoint as regulators often view asset duplication as inefficient and unnecessary. This may lead to a desire to impose passive remedies on BT in place of supporting infrastructure competition and overbuild. For the reasons we outline in this response, we believe that Ofcom must embrace infrastructure competition and promote a model of Efficient Asset Duplication. Any future introduction of passive remedies should not impede this objective.

1.7 Balancing the call for passive remedies with the support of infrastructure competition

We understand that there is widespread support for passive remedies, notably dark fibre, from many CPs. As a provider of dark fibre infrastructure ourselves we fully respect the nature of these requests.

At the same time, rollout of alternative infrastructure by CityFibre and others will take time and is unlikely to cover all of the UK (although with appropriate regulatory environment we believe a large proportion of the UK can be covered). Therefore, Ofcom will need to carefully balance the encouragement of infrastructure competition with potential introduction with passive remedies enforced on BT.

As stated earlier, we do not support the introduction of passive remedies in the 2016-2019 BCMR cycle. Longer term, there may be benefits to introducing passive remedies, however, we propose that Ofcom should set a measure of competitive passive infrastructure rollout that must be achieved before passive remedies are enforced on BT.

For example, a measure that was set at >25% of UK coverage would mean that supply of open dark fibre must be available from suppliers other than BT to at least 1 in 4 potential connections before BT is regulated to supply an equivalent dark fibre product.

This approach has several benefits:

- Encourage CPs to support alternative shared passive infrastructure models – e.g. support CityFibre’s rollout and establish true infrastructure competition.
- Provide a timeframe for CPs to test and migrate to dark fibre solutions without imposing models prematurely that may not scale.
- Provide a timeframe to fully understand the economics of passive infrastructure provision such that any imposed pricing of passive remedies in the future does not undermine the economics of the competitive market.
- Enable Ofcom to better consider any potential changes to regulation that may be needed to support the introduction of passive remedies.
- Enable BT time to recover its common costs associated with past build of active services.

We believe if implemented well, the above proposal that evolves to nationwide passive supply in a way that establishes the competitive market will drive the best outcomes for UK digital infrastructure.

1.8 **Avoiding fear, uncertainty and doubt**

A critical aspect of the debate on passive remedies is the creation of an environment of fear, uncertainty and doubt. FUD may cloud or paralyse decision-making on infrastructure investments or the use of particular forms of connectivity.

New infrastructure builders such as CityFibre may be the most sensitive to the negative effects of FUD in this context – “should CPs consume dark fibre from CityFibre or should they wait until options for passive remedies are formalised and/or introduced?”. Delays in decision-making by CPs waiting for clarity on passive remedies may harm CityFibre’s business in the short to medium term.

Ofcom must take care to ensure that FUD, whether intentional or unintentional, is avoided and that communications regarding this consultation process and outcomes are clear, accurate and concise. This must also include controls on BT to prevent use of FUD in this context to impede the progress of infrastructure competition.

Question 2: Do you agree with our preliminary views on the potential benefits of passive remedies? Please provide evidence to support your view.

- 2.1 CityFibre is a provider of dark fibre products to CPs in all market segments. As such we share many of Ofcom’s view on the potential benefits of passive infrastructure as outlined in section 4 of the Consultation, in particular the dynamic efficiencies outlined in paragraphs 4.11 to 4.22.
- 2.2 Service competition vs. infrastructure competition – Whilst deeper access to BT’s infrastructure may reduce the barriers to CP’s investing further, it must be noted that investment will be at the service layer (through active components and systems) and not at an infrastructure layer (duct and fibre). We would argue that investment in duct and fibre infrastructure is of higher critical importance to longer-term well-being of the UK’s digital infrastructure. We believe passive remedies potentially hinder investment in duct and fibre infrastructure in the short the mid term.
- 2.3 Availability of passive infrastructure transitions more components of the value chain to CPs, potentially allowing for CPs to reduce retail pricing to consumers. However, care must be taken not to undermine the investment case in the passive infrastructure itself. i.e. the investment case for new duct and fibre build must remain compelling.

- 2.4 We broadly agree with Ofcom's comments on the regulatory implication in paragraphs 4.34 to 4.40. However, we feel strongly that the regulatory system must take into consideration the emergence and support of infrastructure competition. The structure of price regulation and charge controls for both active and potential passive remedies must not undermine the investment case for third party infrastructures – in fact we would go further and states that regulatory conditions imposed on BT should positively encourage investment in competitive infrastructure, including the introduction of 'pricing floors'.
- 2.5 No further CityFibre response to Question 2 at this stage in the Consultation.

Question 3: Do you agree with our preliminary views on the impacts and risks of passive remedies? Please provide evidence to support your view.

- 3.1 We have outlined some initial thoughts on risks in our response to Question 1 of the Consultation.
- 3.2 **Risks to investment incentives for CityFibre** – As CityFibre is a provider of passive infrastructure to CPs, the introduction of passive remedies will introduce competition to CityFibre's business model in both our current geographic markets and future geographic markets. BT being mandated to provide duct access or dark fibre clearly affects the competitive landscape for CityFibre with potential negative impacts to our business case for investment.

Without significant further analysis ourselves, and understanding of Ofcom's analysis over time, it is not possible to accurately assess the level of negative impact. Areas of initial concern are:

- **Reduced market share of passive connections** – BT providing passive products in the same geographic markets as CityFibre is likely to reduce the number (or take up) of passive connections we serve. This would have a negative effect on our investment case.
- **Regulated pricing undermines our investment case** – If pricing of passive remedies is set at levels below CityFibre's pricing of passive products then CityFibre's investment case may be challenging or unviable.
- **Fear, uncertainty and doubt delays decision-making** – As stated earlier, FUD may delay CP's decisions to contract with CityFibre and hence negatively impact the take up of CityFibre's passive products in the short to mid term.
- **Stranded investments** – Reduced market share and or reduction in revenues in our current geographic markets may lead to stranded investments and part built networks.
- **Future investments** – Negative impacts to our business case may reduce our incentive for future rollout, thus limiting efficient infrastructure competition in further geographic markets.

- 3.3 No further CityFibre response to Question 3 at this stage in the Consultation.

Question 4: What are your views about the potential impact of passive remedies on the pattern of common cost recovery and the associated distributional impacts?

- 4.1 **Pricing to allow cost recovery should not solely be focused on BT** – CityFibre has made, and is further making significant investments in passive infrastructure. Pricing controls set on BT and the resulting wholesale pricing of BT passive products will directly influence pricing of competing products from CityFibre. Infrastructure investing

has lengthy pay back periods, and CityFibre's cost recovery will be sensitive to take up and pricing. Therefore, in considering any applicable pricing and charge controls we believe it is essential that Ofcom consider the broader competitive market rather than focusing just on BT's common cost recovery.

- 4.2 **Geographic de-averaging could lead to anti-competitive behaviour** – We believe Ofcom must look beyond the issues of arbitrage and consider the dynamics of infrastructure competition on a broader basis. If BT chooses to price passive products based on geography, there is a risk that BT will seek to introduce lower predatory pricing in certain areas it feels it is or could be subject to infrastructure competition, and use higher pricing elsewhere to cross-subsidise such anti-competitive pricing tactics.
- 4.3 No further CityFibre response to Question 4 at this stage in the Consultation.

Question 5: Do you agree with our initial view that mobile backhaul and fixed broadband backhaul are likely to be the primary applications with significant demand for passive remedies?

No CityFibre response to Question 5 at this stage of the Consultation.

Question 6: What benefits might duct access offer over dark fibre and vice versa? Is there a case for having both remedies?

- 6.1 As stated early in part 2 of our response, CityFibre is not currently a user of BT infrastructure. As a provider of dark fibre products to CPs, we may wish to explore the potential to extend the geographic coverage of our fibre networks by gaining access to BT ducts and poles. In such circumstances, access should be unrestricted.
- 6.2 We believe that passive remedies for unrestricted duct access are most relevant in geographic areas where BT have expanded or upgraded its network using State Aid – this being broadly the rural areas where BT has benefited from BDUK funding. This is due to the fact that the high level of state aid intensity BT has enjoyed has already largely undermined the investment case for alternative infrastructure in these areas.
- 6.3 No further CityFibre response to Question 6 at this stage of the Consultation.

Question 7: If passive remedies were restricted to particular product types or geographic areas how might this affect the usefulness and benefits of the passive remedy?

- 7.1 See answer to Question 6.
- 7.2 No further CityFibre response to Question 7 at this stage of the Consultation.

Question 8: What arrangements would be appropriate for the supply of new infrastructure for passive remedies?

Question 9: Do you agree with our initial views about the non-discrimination arrangements for passive remedies?

Question 10: In light of the trade-offs identified, which broad options on pricing do you consider would be most appropriate for passive remedies and why? Please also provide details if there is another pricing approach you consider would be appropriate in light of the considerations identified in this section.

Question 11: If a value-based (active minus) approach to pricing dark fibre were adopted,

what do you think would be an appropriate active wholesale product (or products) to reference?

Question 12: Do you have any other comments on the issues raised in the document or comments that might aid our consideration of the passive remedies as a whole?

No CityFibre response to Questions 8 to 12 at this stage of the Consultation.

--- END OF RESPONSE ---