

Ofcom Business Connectivity Market Review

Further consultation

Response by TalkTalk Group

17 December 2012

TalkTalk is pleased to provide the following responses to the questions in Ofcom's consultation document.

Question 1: Do you have any comments on our proposal to include the Slough sectors in the WECLA?

We believe that Ofcom should ensure that its economic assumptions about the likely reach of alternative networks are based on realistic commercial behaviour in the absence of regulation of BT.

Question 2: Do you have any comments about the proposed amendments to the Proposed SLG Direction?

We note Ofcom's intention to maintain SLG caps for BCMR products which, Ofcom says, were accidentally not included in the original proposals.

We do not understand or agree with Ofcom's brief reasoning in support of its proposal. Ofcom explain at §3.11 that caps are necessary to:

- Avoid exposing 'BT to unlimited financial risk'
- Avoid imposing 'unreasonable burdens' on BT

These points are not correct (in and of themselves) and furthermore even if they were correct they would not justify the imposition of caps due to the negative impact of this mechanism.

The absence of caps does not, in practice, expose BT to unlimited financial risk or impose an unreasonable burden (except in the most hypothetical and unrealistic situation). To show this, it is worth putting some realistic numbers to the situation in relation to the cap on late provision:

- There are about 40,000 Ethernet (WES, BES, EAD, EBD) circuits connected each year (these represent the majority of BCMR).
- Assume 2% (bad case scenario) are delivered more than 60 days late (60 days being the cap) and are instead delivered in 80 days on average incurring 20 days of SLG compensation. The SLG is set at 1 month rental per day late (monthly rental averages about £250 per day). Thus each late circuit incurs a cost of £5,000 (=20 x £250).

- Thus the annual cost resulting from no caps would be £4 million. This is less than 0.03% of BT's expenditure, or £1 in every £30,000.
- If there was a genuine force majeure incident that has caused these delays then that event would provide BT a 'get-out' in any case. Indeed our experience is that BT is very keen to declare MBORC (Matters Beyond Our Reasonable Control) as soon as possible when weather conditions change.

We therefore cannot understand how Ofcom has reached its conclusion – there is not an unlimited financial risk in any meaningful sense and such a relatively small amount can hardly be described as an unreasonable burden. In reality the cap is just a way of BT increasing its profits at the expense of CPs and customers.

In contrast, there are genuine negative economic consequences of a cap on SLG. Most importantly a cap weakens BT incentives to perform to an acceptable quality level and leaves CPs bearing the cost of BT inadequacies – for example, once BT has missed the CRD/CDD date by more than 60 days there is hardly any incentive to deliver the circuit expeditiously. Ofcom is fully reviewing the issues relating to SLGs for LLU services in the context of the Wholesale Local Access Market Review. It is disappointing that Ofcom is not taking the same complete and rounded view in the BCMR and is instead just looking to rubberstamp its assessment from over 4 years ago.

Question 3: Do you have any comments about our proposal that BT should be subject to cost accounting obligations and not required to publish DLRIC & DSAC figures?

We are pleased that Ofcom is proposing to require BT to provide cost accounting data. However, this does not go far enough. In particular, the DSAC and DLRIC costs (for each product) will only be made available to Ofcom. The DSAC/DLRIC numbers must be published else CPs have no way of monitoring Openreach's pricing behaviour.

DLRIC/DSAC numbers are relevant to the cost orientation concept. Ofcom's position is effectively that for prices to be cost orientated they need to be below DSAC (and above DLRIC). Ofcom has not though imposed a cost orientation obligation because, it says, the design of the charge control combined with the starting prices will mean prices should remain below DSAC. This is clear from Ofcom's comment at §4.22

In the proposed charge controls, sub-caps are used to constrain the movement of individual charges, effectively purporting to replace the function previously performed by cost orientation obligations.

Therefore, it is Ofcom's clear intent that prices remain below DSAC (even though there is no cost orientation obligation). However, by not publishing the data CPs cannot monitor whether prices are or remain indeed below DSAC¹ and take action if required (perhaps based on a non-discrimination obligation). Given Ofcom's track record, we have no

¹ Ofcom has claimed that prices are currently below DSAC (though they have not yet provided the evidence to support this claim). Further Ofcom has not provided any analysis to show that prices (sub-capped at RPI-RPI will remain below DSAC (which is likely to fall at around 10% per year). If this evidence and analysis were published then it may reduce the need for ongoing publication of DSAC.

confidence that Ofcom would take proactive action itself in the case where prices are above DSAC. Indeed, prices on Ethernet circuits were above DSAC for years without Ofcom taking any action until CPs lodged disputes following breakdown of negotiations with Openreach.

We can see no cost or downside from Openreach's perspective from continuing to publish DSAC/DLRICs. The numbers are prepared anyway (since BT would notify them to Ofcom) so there is no additional preparation cost. Further, there can be no confidentiality concern; the figures are based on such a convoluted algorithm that means that no underlying cost information (e.g. regarding particular contract prices) can be derived; and, furthermore, these figures have been published for many years in the past and no concerns have been raised.

We therefore believe Ofcom needs to rethink its proposals and ensure that DLRIC and DSAC information is available to CPs to ensure they can verify the cost patterns of Openreach and check for unreasonable pricing behaviour.

Question 4: Do you have any comments about the proposed TAN definition or the proposed circuit routing rules?

We believe that the proposed TAN definition and circuit routing rules appear reasonable although Ofcom must ensure that Openreach does not engage in behaviour to restrict unreasonably the commercial freedom of CPs.

Question 5: Do you have further evidence on competition in the MISBO market outside the WECLA, including the use and impact of dark fibre?

We have no further evidence in this area. We would caution against relying on any market evidence submitted by BT. Ofcom must ensure that it collates market data through objective and independent sources before forming a final view on whether BT has SMP in the MISBO market outside WECLA.