Everything Everywhere's response to Ofcom's Consultation on maximum Service Charges for 09 and 118 services in the unbundled tariff regime

Non-Confidential

19 September 2012

Table of contents

1 Introduction and background

Everything Everywhere ("EE") welcomes the opportunity to comment on Ofcom's latest Non-Geographic Call Services ("NGCS") consultation ("the Consultation"), which sets out Ofcom's options for setting maximum service charge caps for 09 and 118 services under the proposed unbundled tariff regime.

Using Ofcom's own framework of analysis EE thinks that the maximum service charge caps under Option 1 should be the preferred approach. Option 1 offers material additional headroom for 09 service providers ("SPs") to encourage further entry, while minimising the risks to consumer welfare of:

- higher bad debt (and distortions to competition via a higher Access Charge ("AC") in order to try to counteract this bad debt risk);
- distortions to competition for mobile short code services;
- a greater fraud risk; and
- bill shock.

For these reasons EE argues that Option 1 maximises welfare outcomes for both competition and consumers.

The proposed unbundled tariff regime

Ofcom's detailed proposals on the proposed unbundled tariff regime (published in April 2012) involve splitting (and making transparent to consumers on their bills) the money that is paid to fixed and mobile operators (the access charge - AC) and the total retail charge. The total retail charge will include the AC and the remaining money that is paid to the fixed terminating provider to cover the costs of routing and managing the non geographic call, and payment for the service the consumer is receiving (the Service Charge ("SC")).[1]

EE's response to those proposals was provided to Ofcom in July 2012. EE does not propose to repeat the submissions in that response here. However, of particular relevance to the current consultation are the concerns that EE has raised regarding Ofcom's proposal to only allow the setting of a single AC, across all 08, 09 and 118 calls, despite significantly higher retailing costs on 09. As noted in EE's July 2012 consultation response, by removing the commercial flexibility for originating communications providers ("OCPs") to respond to higher (or greater variability) in 09 retailing costs via separate ACs for the 08 and 09 ranges, Ofcom increases the commercial exposure faced by OCPs, which will in practice be compensated for through higher overall ACs. EE remains of the view that this will distort competition and harm the best interests of consumers. Each of the options proposed in the current consultation is likely to increase the cost of calls to 09 numbers, and hence exacerbate this problem. These considerations should motivate Ofcom first to revisit its proposals for a single AC and secondly to choose option 1 over options 2 and 3 in terms of the level of the 09 and 118 SC, as this option will have the least inflationary effect on the SC, and thus also on the AC.

Maximum SC charges for 09 and 118 services

Ofcom is now proposing in the Consultation to undertake further regulatory intervention on the SC element of 09 and 118 charges by:

- on the one hand, undertaking regulatory changes to BT's NTS call origination condition to facilitate a higher SC payment to 09 and 118 SPs to encourage greater entry of value added 09 and 118 services
- while at the same time providing backstop price protection in the form of maximum SC caps on 09 and 118 to minimise the risk of fraud, bill shock and bad debt.

Ofcom argues that current outpayments to SPs are too low and that its proposals to allow more "headroom" will encourage more value added 09 and 118 services for consumers (i.e. "more for more"). EE rejects Ofcom's claim that SPs do not already receive sufficient payments, since this would necessarily

[1] Communications providers will also need to make the AC and total call charge information available at point of sale and in marketing literature in addition to billing information.

imply limited service offerings on 09 and 118. There is clearly a wide proliferation of 09 and 118 services and range in the quality of services.

EE welcomes Ofcom's recognition that if the SC element increases there is a risk of greater fraud, bill shock and bad debt and therefore is proposing maximum SC caps. However, EE believes that Ofcom's Consultation consistently overstates the aggregate benefit of value added entry by SPs while consistently understating the inherent magnitude of risks of higher bad debt, fraud and bill shock. Ofcom's proposals also risk diminishing price competition by creating incentives for outpayments to cluster at the maximum SC cap.

For these reasons EE does not support Ofcom's preferred "middle ground" Option 2 (a maximum cap of £3 per minute or £5 per call, ex VAT) nor the "upper bound" Option 3 (a maximum cap of £5pm or £10pc, ex VAT). Both options would appreciably raise the likelihood of higher ACs to compensate for heightened commercial exposure to increases in retailing costs and impact on consumers through fraud and bill shock.

The risks attached to the lower SC caps under Option 1 (a maximum cap of £2.29 per minute or £2.29 per call, ex VAT) could be manageable. But even these risks may not be manageable on a business as usual basis and may result in additional resource costs for EE and do not entirely mitigate fraud, bad debt or bill shock risk.

2 EE comments on and analysis of the Consultation proposals

2.1 Introduction to comments and analysis

In this section, EE comments on the methodology used by Ofcom to assess maximum SCs for unbundled 09 and 118 services under Options 1, 2 and 3. We also explain why EE considers lower caps under Option 1 (and not Ofcom's preferred caps under Option 2) are more likely to maximise overall welfare outcomes for competition and consumers.

A key justification for Ofcom's proposals in the Consultation is that retail calls to 09 numbers from BT have been capped in nominal terms at £1.53 per minute since 1997, and it remains the benchmark retail price including for all fixed OCPs. Ofcom argues this has lead to a de-facto constraint on outpayments to PRS organisations of no more than £1.45 per minute for calls. Ofcom considers that this restriction on outpayments constrains the range of services offered over PRS to the detriment of consumers and should be lifted.

However, while Ofcom argues that its proposed tariff unbundling regime will naturally constrain SCs on 09 and 118 through greater pricing transparency and competition, Ofcom argues it is in the interests of consumers to minimise the risk of fraud, bad debt and bill shock by additionally imposing backstop price protection in the form of a maximum SC cap. Ofcom is considering the following three options:

Option 1: a maximum cap of £2.29 per minute or £2.29 per call

Option 2: a maximum cap of £3 per minute or £5 per call

Option 3: a maximum cap of £5 per minute or £10 per call (plus a pre-call announcement of the SC)

Ofcom's present assessment is that Option 2 is the preferred option by applying the following six criteria:

(1) transparency/consumer awareness

(2) efficiency of pricing

(3) service quality variety and innovation

(4) access to DQ at an affordable price

(5) consumer exposure to fraud and bill shock,

(6) OCPs' exposure to bad debt.

EE disagrees with Ofcom's assessment and choice of Option 2. EE re-assesses Options 1, 2 and 3 under each of these criteria below and explains that when all costs and risks are fully accounted for, Option 1 represents the appropriate trade-off between these criteria, because it maximises welfare outcomes for competition and consumers.

2.2 Transparency/consumer awareness

Ofcom's view

Ofcom concludes that Option 2 would lead to a lower number of price points than Option 3 and will therefore further increase consumer pricing awareness (see paragraph 4.159). However, Ofcom appear to view Option 1 and Option 2 as equally satisfying this criterion when they also state at paragraph 4.128:

"In deciding the most appropriate level for the cap, we need to consider that higher caps (e.g. in option 3) could potentially lead to a greater number of pricing points than lower caps (e.g. Option 1 and 2)."

EE's view

EE does not think Ofcom is in a position to assess the extent to which the range of 09 and 118 price points might mitigate the maximum SC cap effect on price awareness because the price points have not yet been agreed. Of the 20 or so price points, they may be evenly spaced across existing outpayments to the maximum SC values. However, they may cluster at 1ppm intervals below the maximum cap (such that the range of 20 price points lies between £2.80 and £3.00 per minute under Option 2. Clearly these two extreme approaches to identifying the 09 and 118 price point ranges would have very different impacts on the price awareness effect of having a maximum SC - i.e. if the price points are distributed evenly then a higher SC would imply that the cap will have reduced value for price awareness purposes, whereas if they are all clustered towards the top of the range then the cap will be more meaningful for price awareness purposes, even if set at the highest proposed levels under option 3. It is difficult to make predictions about this until the price points have been set by Ofcom following the conclusion of the industry working group process. However, working purely from theoretical possibilities, all other things being equal Option 1 is likely to offer the strongest consumer benefits in terms of price awareness[2], Option 2 the next highest benefits and Option 3 the lowest benefits.

Given these uncertainties and risks, EE considers only Option 1 satisfies this criterion because it involves the least significant one-off increase in the SC and therefore will least adversely impact on consumer price awareness.

2.3 Efficiency of pricing

Ofcom's view

Ofcom make the following key statements in their assessment of efficient pricing:

Consumers benefit from prices that do not distort their consumption or subscription decisions (paragraph 4.19)

and

In deciding the best approach for the SC for 09 and 118 calls we need to ensure that our proposals are consistent with consumers' preferences and expectations on the prices for these number ranges (paragraph 4.21).

Further Ofcom argues:

A key question to assess the benefits of a higher cap is therefore to understand whether there is consumer demand for services requiring higher prices (in which case a higher cap may be preferable) (paragraph 4.130).

---

[2] Although acknowledging that setting the SC cap at the level of the current BT retail price cap would be even better in this regard than Option 1.

Ofcom argues that Option 2 would satisfy this criterion because there is likely to be unmet demand at these maximum SCs on the 09 range at current prices. It does not provide any direct evidence of this.

Ofcom estimates the efficient maximum SC cap by examining the retail prices paid by consumers of services offered on mobile short codes (up to £5-£10 per call for charity donation services).

Ofcom argues that these prices provide an efficient benchmark for setting a maximum SC for NGCS reflecting the potential unmet demand on the 09 number ranges. Ofcom does not separately consider this issue in respect of 118 services.

Importantly, Ofcom recognises that an element of the price charged to the end-customer for calls to mobile short codes is retained by the originating mobile operator. Accordingly, Ofcom acknowledges that setting the SC for 09 at the same level as the maximum retail prices charged to customers for the use of short codes (at £5-£10) would necessarily imply a higher outpayment to 09 SPs than would be the case if they used a shortcode set at this retail price point - and thus that this would create distortions by creating incentive for SPs to migrate from shortcodes to 09. Accordingly Ofcom argues the benchmark analysis supports an efficient maximum SC cap under Option 2 (but leads it to reject Option 3).

EE's view

EE disagrees with Ofcom's analysis and conclusions in so far as this analysis leads Ofcom to prefer Option 2 over Option 1. EE does not offer commercial services on mobile short codes at the retail prices referred to by Ofcom in the Consultation (paragraphs 4.130-4.139). The claim that there is "unmet demand" on 09 on at these higher price points under Option 2 therefore seems misplaced since higher priced mobile shortcodes are not being used. SPs of shortcodes typically base their mobile shortcode service on the concept of a lower upfront single payment as it provides consumer confidence and certainty. Acccordingly SPs are happy with less revenue than would be the case under Option 2.

EE provides access to commercially oriented services on short codes at retail price points up to £1.50 per call on Orange and £2 per call on T-Mobile. Although EE does provide access to short codes for some charities (such as Comic Relief) with donations payable of £5-£10 per call, these are not representative of retail prices for commercially oriented services. EE understands the price points of £1.50 and £2 per call are also the highest across all other mobile networks (otherwise the industry would have demanded these higher prices from EE and we would have received such requests from aggregators). Accordingly, Ofcom's analysis that suggests there is unmet demand for commercial services at the retail prices of £5-£10 on the 09 range is flawed since these relate primarily to prices of a limited number of charity services.

EE currently offers outpayments on mobile short codes used for commercial services of around [Confidential] for Orange which implies an SC of [Confidential] and [Confidential] for T-Mobile which implies and SC of [Confidential]. A percentage of this payment will be retained by the aggregator (as a fee) and a proportion by the TCP before the remaining revenue share is passed through to the SP. Under Option 2 a maximum SC of £3 per minute or £5 per call on 09 (ex VAT) clearly provides higher outpayments compared to current outpayments on short codes. EE reiterates that current pricing on mobile short codes provides no evidence of unmet demand on 09 at the higher price points under Option 2.

If Ofcom proceeds with Option 2 (or even worse Option 3), we are also concerned that this may encourage inefficient migration of SPs away from short codes to 09. The mobile short codes market is an example of a market which demonstrate how industry can lead to innovative solutions that deliver real benefits to UK consumers and businesses and Ofcom should be loath to adopt policy solutions which may inefficiently distort competition in this successful market. For instance:

- Short codes are unique because they offer a single up front price for the customer, which removes any uncertainty over price. Even under Ofcom's proposals, customers will in many cases rely on TV voting announcements prior to a commercial break setting out the SP's charge but that "access charges may vary between networks".
- [Confidential]

Option 2 clearly undermines growth in these market based innovations.

In setting a maximum SC to encourage services to meet the unmet demand, Ofcom may inadvertently incentivise all SPs to price up to this level, regardless of the value added, which would not be allocatively efficient.

For instance, one of the inherent dangers of setting maximum price caps in markets is that caps can diminish price competition and encourage clustering of prices at the maximum, especially if these can be justified as 'sanctioned by the regulator'. Willingness to pay and competition arising from unbundling could discourage this practice, as 09 services tend to be more discretionary and arguably more elastic than other NGN services (e.g. compared to 08). However, unless price elasticity of demand is sufficiently elastic and consumers in practice use the services frequently enough to change SP or compare similar or substitutable services (all of which are yet untested propositions) it seems more likely that Ofcom's consolidation of 09 price points (to around 20) in combination with maximum SC caps will simply be used as an opportunity by many if not all SPs to ratchet up to the maximum SC allowed (regardless of value added service content). Certainly there is likely to be a sub-set of customers calling 09 numbers who are effectively "locked-in" - such as those seeking to call to vote on a particular reality television program. EE considers that the special characteristics of demand and competition for NGCS have not been given sufficient weight by Ofcom. Accordingly, EE believes that Ofcom's test of efficient pricing focused solely on the potential for the different Options to meet unmet demand is flawed, as it does not also factor in the risk to efficient pricing of a clustering effect and the allocative inefficiencies that this would generate.[3]

The recent introduction of maximum price caps on international retail roaming charges provides an example of the potential perverse impacts price caps can have on efficiency. Maximum price regulation has provided a 'focal point' such that most UK mobile operator's retail roaming prices are now clustered at the maximum rates, which has distorted the potential benefits of price competition for UK mobile customers.

Ofcom's analysis that only a few SPs currently choose prices at levels consistent with the SC caps proposed under Option 2 provides no evidence that a focal point would not arise (paragraph 4.138). Setting a maximum cap will change the competitive dynamic for pricing in the market by sanctioning price rises for all.

For all these reasons EE does not consider that this criterion supports either Option 2 or 3. Only Option 1 satisfies this criterion, since even if all prices clustered to the maximum it would generate the least allocatively inefficient outcome of all the options (since the difference between the lowest value added services and the maximum SC charge would be minimised, if such services were priced at the maximum SC).

2.4 Service quality variety and innovation

Ofcom's view

Ofcom concludes that Option 2 is most likely to promote innovation by SPs (paragraph 4.149) and that Option 1 would not offer sufficient headroom (paragraph 4.159).

Ofcom has ruled out further consideration of setting the maximum SC at BT's current maximum retail price of £1.53 per minute on the grounds that the de facto outpayment consistent with this price currently restrict entry of value added PRS SPs, citing the erosion of the price in real terms since 1997 (paragraph 4.91) and evidence provided by ITV and AIME on the potential for entry by higher prize value competitions, more engaging competition formats and higher value entertainment services from higher SC caps (paragraphs 4.190-4.149).

EE's view

EE remains sceptical of the ability of any of the new SC caps proposed under Options 1 to 3 to stimulate a material increase in the number or quality of 09 or 118 services above current levels.

3 The law of one price states allocative efficiency is best served when consumers face a single price for homogenous goods. Conversely, the same or a uniform maximum price (or clustered prices) would not promote allocative efficiency for heterogeneous sets of different value added services.

There is clearly currently a wide proliferation of 09 services and range in the quality of services. In particular, there appears to be a proliferation of profitable TV competition and entertainment formats with voting services offered across the UK on 09 numbers under the present arrangements (eg X-Factor, Britain's Got Talent, Big Brother, the Voice etc).

However, as Ofcom has noted in its April 2012 consultation[4], these services now compete with a range of other services available over a range of technologies, most notably internet and "app" based services. Consumers now have a wide range of options for receiving these services such as voting through a red button, and getting their horoscope delivered by email or a website or twitter. The growth in the smartphone market indicates that such use of such technologies will only increase. Accordingly, pressure from these competing technologies on the incentives of new 09 and 118 SPs to enter the market will only increase in the coming years.

In this market environment, EE believes that the most likely outcome of increasing the SC will simply be to make these existing 09 and 118 services more profitable for existing SPs, rather than stimulating any material degree of new entry. Given this, EE believes that Option 1 represents the best option for UK consumers - providing a marked increase over the current retail price caps to ensure that existing SPs can continue to profitably provide their services and that new SPs can equally enter this profitable market, whilst at the same time keeping a check on the retail price inflation that is likely to flow from either Options 2 or 3 - which is likely to harm the interests of consumers and discourage their use of 09 and 118 services. In this context, it is also important for Ofcom to remember that significantly higher prices for the same or similar 09 and 118 services as those currently available will simply drive consumers to alternative modes of provision, and hence there would be little practical benefit from higher SC caps. This can be seen, for example, by the steadily increasing termination rates charged by The Number UK for its 118 118 service and the corresponding decline in the volumes of calls over the same period[5]

EE notes the evidence presented by Ofcom at paragraph 4.83 which suggests that "the top ten most used tariffs in the 09 range (representing 78% of total terminating traffic on this range) are made up of 7ppm or 3ppc (i.e. drop charge) tariffs".

EE is surprised at these statistics, as the [confidential].[6]

As per NCCN 1107, the (non-ladder charge) termination rate payable to BT for calls to numbers in the P10 charge band are as follows:

Daytime ppm	Evening ppm	Weekend ppm
29.1870	29.5203	29.5678

As per NCCN 1107, the (non-ladder charge) termination rate payable to BT for calls to numbers in the P7 charge band are as follows:

Daytime ppm	Evening ppm	Weekend ppm
52.7978	53.0870	53.2370

Even if the SC was to be set at exactly the level of the current BT retail cap for calls to 09 numbers of £1.53, this would represent an approximate three-fold increase on the highest termination rates listed above. At £2.29 ex VAT (the cap proposed under Option 1), this maximum SC would represent approximately 7.6 times the (non-ladder charge) termination rates currently payable for calls in the P10 charge band and 4.3 times the (non-ladder charge) termination rates currently payable for calls in the P7 charge band. Accepting Ofcom's evidence, this cap would also represent an increase of more than 30 times the 7ppm rate referred

[4] http://stakeholders.ofcom.org.uk/consultations/simplifying-non-geographic-no/

[5] http://stakeholders.ofcom.org.uk/binaries/consultations/simplifying-non-geo-numbers/responses/Everything_Everywhere.pdf, paragraphs 5 (c) and 14.

6 See annex 9.2 to EE's Dispute filing on NCCNs 1101 and 1107

to in paragraph 4.83 of the Consultation. It is hard to see how there would not be sufficient headroom under such caps to both adequately compensate existing 09 providers and stimulate new entry.

EE therefore considers that given the risks inherent in higher SCs (see below), Ofcom should implement Option 1 and observe value added entry (with minimal risk) over a reasonable period and then re-assess the maximum SC caps under option in the event it considers the headroom remains insufficient.

2.5 Access to DQ at an affordable price

Ofcom's view

Ofcom states the following at paragraph 4.75:

"the Universal Service Directive requires us to ensure that directory enquiry services are available to all UK consumers at affordable prices. However, while we believe that the best way to ensure that there is access to 118 services at affordable prices is through the proposed imposition of the unbundled tariff and its likely impact in promoting competition in this number range, we note that in an environment of regulatory change, a cap would limit the risk of SPs subjecting consumers to exploitative prices that are not consistent with our obligations. For the reasons discussed above we consider that a maximum SC should also apply to 118 numbers."

Ofcom assesses that Option 2 is likely to promote the affordability of directory enquiry services to a greater extent than Option 3.

EE's view

Ofcom argues that under Option 2 only 4 out of 80 charge bands would exceed the maximum caps (Table 4.3). Under Option 1, the vast majority of traffic terminated on 118 would continue to show outpayments below the maximum SC caps under Option 1 such that these maximum SCs would not discourage existing SPs from continuing to provide the service (eg on the more popular directory enquiry numbers.

For example, approximately [confidential] of minutes originated by EE on the 118 range are on The Number UK (TNUK) (118 118) and BT (118 500).The termination charges we pay out on these calls include both drop call and per minute charges and are [confidential]. This indicates that additional headroom would still be available under Option 1 (i.e., £2.29 per minute and £2.29 per call, ex VAT).

This more proportionate approach to examining the most popular 118 numbers would be likely to suggest Option 1 would not discourage the reputable, successful and profitable providers in the market.

EE accepts that Option 1 will involve setting a cap that is lower than current termination rate price points on some additional 118 charge bands than would be the case under Option 2. However EE by no means considers this to be a bad thing. In particular, it means that Option 1 would necessarily promote affordability for 118 services even more so than Option 2. Lower prices may also stimulate greater volumes of calls to 118 numbers, which will benefit both consumers and DQ SPs.

2.6 Consumer exposure to fraud and bill shock

Ofcom's view

Ofcom recognises that consumers use NGCS infrequently and hence are more susceptible to bill shock if the SC increases. Ofcom also recognises that the move to an unbundled tariff regime may initially create some customer confusion and SPs may seek to take the opportunity to exploit this confusion by raising the SC during the period of regulatory change heightening the risk of bill shock.

Ofcom further highlights "the potential for raising high revenues on 09 and 118 services makes them an attractive target for fraudulent users", although Ofcom argues fraud tends to be more common on other number ranges (see paragraph 4.25).

EE's view

EE shares these concerns and is pleased that Ofcom has recognised the potential risks of regulatory change. However there are three important gaps in Ofcoms analysis that bias it towards Option 2, when Option 1 would be the more appropriate response to these risks.

First, Ofcom focuses solely on the direct impact of fraud on consumers and has ignored the impact of fraud on communications providers, who spend considerable resources to detect fraud including in cases where no PRS service is in fact available to consumers. Ultimately, such costs of fraud detection and prevention incurred by communications providers also need to be recovered from consumers.

- For example, there are schemes whereby no PRS service is provided by individuals or organisations who purchase NGCS numbers and attempt to artificially inflate traffic (AIT) by setting up calling loops (e.g. using autodialing equipment) to generate the outpayments to themselves.
- EE presently has methods for detecting this type of activity, [confidential].
- However, the issue for EE is that even under Option 1, we expect a considerable increase in the amount of fraudulent activity of this kind, which will in turn require a significant scaling up of our fraud detection teams. While it is difficult to predict the precise increase in AIT under Option 1, an indicative estimate is that a doubling of the incidence of fraud might require an additional 5 full time employees to be allocated to this task across the two brands.

Second, Ofcom focuses solely on the direct impact of bill shock on consumers and has ignored the impact of bill shock on communications providers, who will need to expand inbound call centre call capacity to response to complaints arising from bill shock. Again, the costs incurred by communications providers will ultimately be passed on to consumers.

It is naive to think that in response to high SCs and bill shock customers will contact the SP in the first instance. Even where information is provided to direct customers to call the SP, customers will always contact their communication provider first (as communications providers issue the bill). Calls of a complaint nature tend to be of longer duration and hence represent a more significant cost burden on our call centres. In addition to this direct cost, there are indirect costs (i.e. opportunity costs), because increased calls arising from bill shock means EE cannot service and support existing and potentially new subscribers while sales representatives are tied up on calls related to bill shock.

These higher costs will ultimately be borne by consumers in the form of longer call waiting times when seeking customer support services (i.e. poorer customer experience) or even higher retail prices where increased call volumes increase incremental call centre costs (which will be borne industry wide and are unavoidable costs).

Third, Ofcom assumes that opportunism to exploit confusion during the transition by increasing the SC will be temporary, as the proposed unbundled tariff regime will correct this over time as it fosters greater transparency and competition. But as explained by EE under the efficiency criterion (Section 2.3), there is potentially a more permanent incentive for 09 and 118 SPs to cluster their prices at the maximum caps due to the lower price elasticity of demand for NGCS on these ranges and also the largely untested assumption that consumers use these services frequently enough to change behaviour or that they compare similar or substitutable 09 and 118 services.

This suggests that fraud and bill shock may not be a "one off" event arising from few opportunistic SPs exploiting a transitional period and raising prices, but rather high prices (and consequently fraud and bill shock) become a permanent feature of the proposed new regime. Given Ofcom's concerns around bill shock its proposals seem somewhat incongruous.

Accordingly, given the additional costs set out above, and the likelihood of price clustering at the maximum, Option 2 cannot be argued to minimise fraud and bill shock risks for consumers. EE argues Option 1 best satisfies this criterion.

2.7 Communication providers' exposure to bad debt

Ofcom's view

Ofcom concludes that Option 2 better satisfies this criterion than Option 3 (see paragraph 4.159) but also concedes that both Option 1 and 2 may have an advantage over higher caps (i.e. Option 3) in mitigating distortions arising on ACs from bad debt (see paragraph 4.156)

Ofcom states the following at paragraphs 4.55 and 4.56:

"...the level of the SC is likely to affect the extent of bad debt costs. In the absence of a cap, it is possible that the average SC level across all SPs in the 09 range would be higher than it would be if a cap were imposed. This would in turn increase both the likelihood and level of bad debt costs. To compensate for any losses from increased bad debt costs, it is likely that OCPs would raise the level of their ACs and thereby adversely affect the ability of the unbundled charge to secure more efficient prices for calls to non-geographic numbers."

"We therefore consider that a SC cap may be preferable to limit the extent of bad debt and to limit its distorting impact on OCPs' ACs."

Ofcom then argue that a lower cap (Option 1 or Option 2) may have an advantage over Option 3.

EE's view

EE disagrees that Option 2 sufficiently minimises the potential distortionary effect of bad debt on the setting of the AC.

A practical example brings into sharp relief the appreciable risk of Option 2 for bad debt.

At a maximum SC cap of £3.60 per minute (including VAT), this would mean a 77ppm 09 call (from a T-Mobile tariff plan) would increase to £3.76 per minute. This would mean that a 5 minute call would increase in cost to £18.80 (compared to £3.85 today).[7]

This could generate further bad debt if these 09 services are consumed proportionately more by those customer groups who can't pay (e.g. students, migrants, pensioners or unemployed), those who won't pay (e.g. people with no desire to maintain a good credit record) or those who (untruthfully) argue fraud (e.g. argue someone else used their phone without prior authorisation).

EE also notes that increases in the number of customers who cannot or will not pay may mean those customers lose access to other mobile telephony services (as they will be disconnected for non-payment and we will seek to recover, where possible, unpaid amounts through debt collection agencies). Accordingly, higher SCs and therefore higher retail charges on 09 and 118 could have externality effects where disconnected customers unable to make/receive ordinary voice calls or access the internet.

EE notes that in the current economic climate, macroeconomic conditions could also exacerbate bad debt on 09 and 118 numbers. While EE accepts that Ofcom should be concerned with the incremental impact of its proposals for SC caps, there is a real risk that 09 and 118 price rises contemplated by Ofcom, combined with current macroeconomic conditions, could have a multiplicative effect on bad debt on 09 and 118 calls

[7] Under NCCN 1107.

(e.g. higher levels of overall debt and higher unemployment levels might make it harder for these consumer groups to pay higher 09 and 118 charges in the future).

EE recognises that in theory its pay-monthly customers are bound to pay their bills under contractual terms and conditions, and in cases of non-payment, we can refer cases to debt collection services. However, going forward, the reality may be less straight forward. The impact of Ofcom's proposal is unpredictable because we do not have a precedent for such significant increases in outpayments. Although as a communications provider we understand broadly the aforementioned customer groups that are most likely to generate bad debt, it is difficult to know which 09 and 118 services they use, or whether the charges for these services will be set at the maximum SC charges or not. If they do face the higher charges, bed debt risks could increase.

EE is especially concerned that many operators will price 09 and 118 services to the maximum cap level (for the reasons given in section 2.3). Where prices for many 09 and 118 services cluster at the maximum SC cap, we believe this could have more serious implications for bad debt since customers groups with an inherently higher bad debt risk will statistically be more likely to face higher 09 and 118 bills.

EE views Option 1 as the option that minimises the bad debt risk to OCPs, and thus best minimizes the potential negative flow on effects of this risk for consumers.

3 Responses to Ofcom consultation questions

Question 4.1: Do you agree with the assessment criteria we are proposing to use for our analysis, and in particular the three additional criteria we have identified as relevant?

EE agrees with the six criteria but argues that all criteria support Option 1.

Question 4.2: Do you agree that a maximum SC should apply to 09 numbers for the reasons set out above?

Yes. EE agrees that SC caps should be imposed under Option 1 for the reason set out in Section 2 of EE's response.

Question 4.3: Do you agree that a maximum SC should apply to 118 numbers for the reasons set out above?

Yes. EE agrees that SC caps should be imposed under Option 1 for the reason set out in Section 2 of EE's response.

Question 4.4: Do you agree that a different maximum SC for calls charged on a per call basis and calls charged on a per minute basis is appropriate?

Yes. EE supports the proposal for different maximum SC for calls charged on a per call basis and calls charged on a per minute basis under Option 1.

Question 4.5: Do you agree that we should use the RPI measure of inflation to uplift the BT's current maximum retail price for 09 calls to derive the maximum SC under Option 1?

Yes. EE is supportive of the use of RPI to uplift BT's current maximum retail price for 09 calls to derive the maximum SC under Option 1.

Question 4.6: Do you agree that we should not uplift the SC caps by inflation on an annual basis?

Yes. EE agrees that Ofcom should not inflate SC caps on a regular basis as this is likely to reduce consumer awareness (as well as flow on costs of any changes to price points that result from the adjustment in terms of billing systems and changes to customer information / marketing material etc) and therefore would not be in the best interests of consumers.

Question 4.7: Do you agree that the maximum SC cap should be set exclusive of VAT?

Yes. EE agrees that the SC cap be set ex VAT since the process for updating could be complex and costly. This would not prevent SPs' prices being published inclusive of VAT.

Question 4.8: Do you agree that Option 2 (a £3 per minute and £5 per call cap) is the most appropriate maximum service charge limit for 09 and 118 numbers? If not, please explain why.

No. EE disagrees that Option 2 promotes welfare outcomes for competition or consumers. EE argues Option 1 is the optimal option in section 2 of EE's response.

Question 5.1: Are there any other consumer protection measures we should consider for the 09 and 118 ranges? Please explain why you consider any additional measures you identify might be appropriate.

No. EE considers the current range of measures provided under the PhonePay Plus regulations have worked reasonably well and therefore further consumer protection should only be considered if problems develop under the proposed unbundling regime.

Question 5.2: Do you have any comments on our assessment of the costs and benefits of a pre-call announcement on the 09 and 118 range? Please provide reasons for your view.

EE considers that PCAs may have a negative impact on demand for 09 and 118 services. It is also likely that for short calls, a PCA may impact on the utility of the service where call is short. In some cases, such as short TV voting calls, it may be disproportionate to require a PCA, particularly, when the SC has been advertised on TV.

EE also considers that customers will now potentially be overburdened with information on NGCS. Unbundled SCs on NGCs will have to be provided at point of sale, on billing information and on marketing materials. These will also be advertised on TV programs and websites for various information and entertainment services as well.

As the TCP will be responsible for the PCA (given it relates to the SC and not the AC) EE is not in a position to comment on the costs that might be incurred by the TCP, but notes that costs are likely to have fallen for TCPs compared to previous stakeholder submissions, noting SCs will not vary by OCP and hence the TCP will only need to access information in relation to the SC for the number called.

Question 5.3: If relevant, please provide an estimate of the likely costs that you would incur if a pre-call announcement were implemented on these ranges, taking account of any benefits it may bring.

EE is not a TCP and therefore is not in a position to comment on these costs.

Question 5.4: Do you have any comments on our assessment of the costs and benefits of a consumer opt-in for 09 and 118 numbers? Please provide reasons for your view.

EE agrees with Ofcom's assessment that opt in arrangement is likely to work against Ofcom's stated aims for growing the number range by dampening demand for 09 and 118 calls.

Question 5.5: Do you have any comments on our assessment of the costs and benefits of time-related notifications on the 09 and 118 range? Please provide reasons for your view.

EE considers that including time notifications (i.e. via beep sounds) are likely to be intrusive especially for calls of shorter duration priced at the highest SCs. EE considers that the current PhonePay Plus regulations that require certain calls not exceed £25.54 plus VAT (or that the consumer positively confirms they wish to continue the call beyond that point) provide sufficient protection.

Question 5.6: If relevant, please provide an estimate of the likely costs that you would incur if time-related notifications were implemented on these ranges, taking account of any benefits it may bring.

EE has not been able to quantify these costs, but considers annoyance costs of beeps to consumers could be significant for short duration calls which would offset any potential benefits.

Question 5.7: Do you have any comments on our assessment of the costs and benefits of dedicated number ranges on the 09 and 118 range? Please provide reasons for your view.

While having dedicated higher charge number ranges (eg 09x) might have some appeal as Ofcom notes, consumers are aware of the types of NGCS calls to the second digit but beyond that, will be unlikely to understand the distinct types of services and pricing intention behind a third digit prefix. For these reasons, price awareness might be harmed rather than increased under such an option. It is also not clear this would reduce bad debt, bill shock or fraud risk.

Question 5.8: Do you have any comments on our assessment of the costs and benefits of an extension of the 30 day withhold period on the 09 and 118 range? Please provide reasons for your view.

EE agrees that an extension of the withhold period to 6-8 weeks would be a positive measure as it would give EE longer to manage retention of payments to fraudulent operators. However, the impact of this may be neutral if the amount of AIT or other fraudulent activity increases.

Question 5.9: Do you agree with our assessment that additional consumer protection measures would only be justified if SPs are able to set SCs for services on 09 and 118 with the ranges proposed under Option 3? Please provide reasons for your view, including, if relevant, the measures that you consider would be appropriate.

EE agrees with the general view that SCs under Option 3 may warrant further consumer protection, but that the form of consumer protection may depend on the nature of the calls being made, and hence a priori, it is difficult to assess which consumer protection measures may be most appropriate. Fundamentally however, EE does not believe that the implementation of Option 3 is in the best interests of consumers.

Question 6.1 – Do you agree that the level of the SC should be set at £5 per call and £3 per minute and that no additional consumer protection measures will be required? If not, please provide alternative options and evidence to support your preferred option.

EE does not agree that the level of the SC should be set at £5 per call and £3 per minute (i.e. as per Option 2). EE's preference is for the caps to be set as per Option 1. However, under either Option, EE agrees with Ofcom that no additional consumer protection (beyond those requirements currently enforced under PhonePay Plus regulation) would be required.

Question 6.2 – Do you agree with our proposals in relation to the timing of our proposals for a maximum SC charge for 09 and 118 numbers taking effect? Do you have any comments on our Equality Impact Assessment? In particular do you agree with our view that our proposals for changes to non-geographic numbers are likely to have an overall positive impact on the equality groups identified in Annex 15?

EE does not support Ofcom's proposed tariff unbundling regime for NGCs (as set out in EE's response of July 2012). However, were Ofcom to proceed with the proposals, EE would argue that the maximum SC caps for unbundled 09 and 118 services in Option 1 of this consultation be implemented at the same time (i.e. 18 months form publication of the final statement). EE notes however, that this time period for implementation assumes no material delay between the issuing of Ofcom's final statement on policy matters and the issuing of Ofcom's final statements on all other issues required for implementation - including on legal instruments, and Ofcom's proposals for the 050 and 070 ranges. If there is any more than a few weeks delay in the issuing of these other statements, then the time period should run from the date when the last statement is ssued.

EE has no comment on the Equality Impact Assessment.