



## Mobile call termination

Adoption of revisions to SMP Conditions  
in accordance with the directions of the  
Competition Appeal Tribunal of 8 May 2012

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## Section 1

# Background

### The MCT Statement

- 1.1 On 15 March 2011, Ofcom published its Wholesale Mobile Voice Call Termination Statement (the “MCT Statement”).
- 1.2 In the MCT Statement, Ofcom:
  - 1.2.1 identified separate markets for the provision of call termination services by each of thirty-two mobile communications providers (“MCPs”) to another communications provider, for the termination of voice calls to UK mobile numbers which that MCP has been allocated by Ofcom, in the area served by that MCP and for which that MCP is able to set the call termination charge (each a “relevant market”);
  - 1.2.2 determined that each of the thirty-two MCPs has significant market power in relation to the relevant market in which they operate, and
  - 1.2.3 imposed certain SMP conditions on each of these MCPs, including the imposition of a charge control on the supply of mobile call termination (“MCT”) services by each of Everything Everywhere Limited (“EE”), Hutchison 3G UK Limited (“H3G”), O2 (UK) Limited and Vodafone Limited (“Vodafone”).
- 1.3 The SMP Condition imposing this charge control (“Condition M3”) is contained in Annex 1 to the MCT Statement.
- 1.4 On 25 October 2011, Ofcom modified Condition M3 in order to correct a computational error in the cost model underlying the charge control calculations (the “Modification”).<sup>1</sup>

### The MCT Appeals

- 1.5 On 16 May 2011, Ofcom’s decision as set out in the MCT Statement was appealed by British Telecommunications plc, EE, H3G and Vodafone to the Competition Appeal Tribunal (the “Tribunal”) under section 192 of the Communications Act 2003 (the “Act”).
- 1.6 On 30 June 2011, the Tribunal referred the specified price control matters arising in these appeals to the Competition Commission (“CC”) pursuant to section 193 of the Act.
- 1.7 On 9 February 2012, the CC notified the Tribunal of its determination of the price control matters which had been referred to it (the “Determination”).
- 1.8 On 7 March 2012, EE and Vodafone submitted to the Tribunal that parts of the Determination would fall to be set aside on an application for judicial review pursuant to section 193(7) of the Act.

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<sup>1</sup> See Ofcom, *Modification of SMP conditions contained in Ofcom’s Notification under section 48(1) and 79(4) of the Communications Act 2003 of 15th March 2011*, 25 October 2011

- 1.9 By judgment of 3 May 2012, the Tribunal rejected these submissions and concluded that the Determination would not fall to be set aside under section 193(7) of the Act. The Tribunal also granted Vodafone permission to amend its Notice of Appeal in order to incorporate certain submissions which the Tribunal referred to in its judgment as the “unpleaded points”. The Tribunal therefore decided pursuant to section 193(6) of the Act that the appeals should be decided in accordance with the Determination, save that the CC’s conclusions with respect to the unpleaded points must stand as if they had been pleaded by Vodafone in its Notice of Appeal.

### **Directions from the Tribunal to Ofcom**

- 1.10 On 8 May 2012, the Tribunal made an Order which included the following points:

- “1. This Order adopts the same definitions, and should be read with, the Judgment.*
  - 2. Pursuant to rule 11(3)(c) of the 2003 Tribunal Rules, Vodafone be granted permission to amend its notice of appeal in the manner appended to Vodafone’s JR Grounds.*
  - 3. Pursuant to section 195(2) and section 193(6) of the 2003 Act:*
    - a. the Appeals are decided in accordance with the Determination; and*
    - b. the unpleaded points of the Vodafone Appeal are decided in accordance with paragraphs 7.360 to 7.364 of the Determination.*
  - 4. Pursuant to sections 195(3) and (4) of the 2003 Act, the Statement be remitted to Ofcom with the direction that it implement the Statement in accordance with paragraph 3 of this Order.*
- ...”*

## Section 2

# Revisions to SMP Conditions

2.1 Pursuant to section 195(6) of the Act, Ofcom has a duty to comply with the Tribunal's directions. Ofcom therefore now adopts revisions to the following parts of Condition M3 (as amended by the Modification):

2.1.1 the definition of “controlling percentage”;

2.1.2 the definition of “relevant period”, and

2.1.3 Condition M3.4.

2.2 The revisions are set out below and take effect from 11 May 2012.

“**controlling percentage**” means, in relation to ~~the Third Relevant Period, the Fourth Relevant Period and~~ the Fifth Relevant Period and the Sixth Relevant Period, the amount of change in the Retail Prices Index in the period of 12 months ending on the 31 December immediately before the beginning of that relevant period, expressed as a percentage (rounded to one decimal place) of that Retail Prices Index as at the beginning of that period; reduced by ~~36.7 per cent; =~~

(i) in the case of the Fifth Relevant Period, 46.6 percentage points;

(ii) in the case of the Sixth Relevant Period, 3.0 percentage points;

“**relevant period**” means any of the following –

- (i) the period from 1 June 2011 to 31 October 2011 (the “First Relevant Period”);
- (ii) the period from 31 October 2011 to 31 March 2012 (the “Second Relevant Period”);
- (iii) the period ~~of twelve months~~ beginning on 1 April 2012 and ending on ~~31 March 2013~~ 10 May 2012 (the “Third Relevant Period”);
- (iv) the period ~~of twelve months~~ beginning on 11 May 2012 and ending on 31 March ~~2014~~ 2013 (the “Fourth Relevant Period”);
- (v) the period of twelve months beginning on 1 April ~~2014~~ 2013 and ending on 31 March ~~2015~~ 2014 (the “Fifth Relevant Period”);
- (vi) the period of twelve months beginning on 1 April 2014 and ending on 31 March 2015 (the “Sixth Relevant Period”);

**M3.4** The charge ceiling is –

- (a) for any Call on a day in the First Relevant Period, 2.984 pence per minute;

- (b) for any Call on a day in the Second Relevant Period, 3.015 pence per minute;
- (c) for any Call on a day in the Third Relevant Period, 2.053 pence per minute;
- (d) for any Call on a day in the Fourth Relevant Period, 1.500 pence per minute;
- (e) for any Call on a day in the ~~Third Relevant Period, Fourth Relevant Period or~~ Fifth Relevant Period or the Sixth Relevant Period –
  - a. an amount equal to –
    - i. the charge ceiling, expressed in pence per minute (rounded to three decimal places), in the relevant period preceding the relevant period in which the Call was made; multiplied by
    - ii. the sum of 100 per cent and the controlling percentage for the relevant period in which the Call was made, and is
  - b. expressed as being pence per minute and rounded to three decimal places.

## Annex 1

# Explanatory Statement

A1.1 For reference, Ofcom sets out in this Annex an explanation of how it has calculated the revisions to Condition M3, which are contained in the operative part of this document. Ofcom's calculations are consistent with the proposals set out in its letter to the Tribunal of 2 March 2012, which is referred to at paragraph 330 of the Tribunal's judgment.

## Effect of Determination and Tribunal's directions

A1.2 The combined effect of the Determination and the Tribunal's directions is that the following adjustments should be made to the MCT charge control:

- There should be a three-year glide path which moves from the level of mobile termination rates ("MTRs") at the end of the previous charge control (i.e. on 31 March 2011) to the revised level of LRIC at 1 April 2013, by means of three reductions of equal percentage size on the first of April of each year.
- After the three-year glide path to the LRIC level in 2013/14, there should be a further reduction to MTRs on 1 April 2014 to the level of LRIC for the year 2014/15.
- The LRIC figure used to calculate the revised glide path should be the level calculated for the year 2013/14, taking into account the Modification to the charge control, after correcting the error in relation to Reference Question 6 identified by the CC and, in line with the Tribunal's directions, on the basis that Vodafone's unpleaded points are decided in accordance with paragraphs 7.360 to 7.364 of the Determination.
- The levels of LRIC that result from making these adjustments are as follows:

**Table 1 – Revised LRIC calculations**

*ppm, 2008/09 prices*

	2010/11	2011/12	2012/13	2013/14	2014/15
Revised LRIC figures	0.80	0.68	0.66	0.69	0.67

Source: Determination, Table 7.12

## Calculations underpinning revisions to Condition M3

A1.3 In light of the Determination and the Tribunal's directions, Ofcom has performed two calculations to inform our revisions to Condition M3.

### First calculation - revised glide path

A1.4 Ofcom has undertaken a revised glide path calculation, substituting the end point of the glide path in accordance with the Determination. Specifically, we have used a



LRIC value of 0.69ppm (in 2008/09 prices) in 2013/14 as the end point of the glide path.

- A1.5 The starting point for the revised glide path is the MTR at the end of the previous charge control, i.e. that in force on 31 March 2011. The starting point for the calculation is therefore 4.428ppm, which was the nominal TAC in force on 31 March 2011.
- A1.6 Consistent with the method we used in the MCT Statement, this starting figure is rounded to 2 decimal places (i.e. 4.43ppm) and deflated to 2008/09 prices, so that it is comparable to the end point of the glide path (as calculated by the MCT cost model, and which is itself reported in 2008/09 prices and rounded to 2 decimal places). This gives a starting charge of 4.18ppm in 2008/09 prices.
- A1.7 The end point for the revised glide path is the revised level of LRIC for 2013/14 taking into account the Modification to the charge control and the error which the CC identified in relation to Reference Question 6, and on the basis that the corrections arising out of Vodafone's unpleaded points are made. As set out in Table 1 above, the end point is therefore 0.69ppm in 2013/14 (2008/09 prices, 2 decimal places).
- A1.8 The revised glide path should move from the starting point to the end point by means of three reductions of equal percentage size, on the first of April of each year.
- A1.9 Consistent with the method adopted in the MCT Statement, the percentage reduction is calculated in two stages:
- A1.9.1 the real reduction ('Y') required to move from the start point to the end point in three reductions of equal percentage size is calculated. This calculation gives a Y-value of -45.14%.
- A1.9.2 a geometric conversion is then applied to the real Y-value. The geometric conversion factor is 3.26%<sup>2</sup>, which gives an X-value of **46.6%** (rounded to 1 decimal place). This is the constant 'X' value used in the RPI-X formula for the three-year glide path.
- A1.10 It is possible to perform the RPI-X calculation set out in Condition M3 to derive the revised nominal charge ceilings for the first two years of the charge control (2011/12 and 2012/13) as the relevant RPI figures are available.<sup>3</sup> The revised nominal charge ceiling for 2011/12 is 2.577ppm and the nominal charge ceiling for 2012/13 is **1.500ppm**.

### Second calculation – final year's charge ceiling

- A1.11 There should be a further reduction to MTRs on 1 April 2014 from the level of LRIC for the year 2013/14 to the level of LRIC for the year 2014/15.

<sup>2</sup> Consistent with the methodology adopted in the MCT Statement, we have used a geometric average over the number of years in the glide path (in the MCT Statement, four years; in this case, three years) using actual inflation (i.e. RPI for the immediately preceding calendar year, which was 4.8%) for the first year (2011/12) and forecast inflation (of 2.5%) for the remaining years.

<sup>3</sup> The value of the percentage change in RPI used in the controlling percentage for the charge control year 2011/12 is 4.8%. This is given by the change in RPI for the year to December 2010. For the charge control year 2012/13, the percentage change in RPI used in the controlling percentage is also, by coincidence, 4.8%. At the time of the Modification (published on 25 October 2011), the change in RPI applicable to the controlling percentage was only available for the charge control year 2011/12.

- A1.12 As set out in Table 1 above, the level of LRIC for the year 2013/14 is 0.69ppm and the level of LRIC for the year 2014/15 is 0.67ppm (both in 2008/09 prices).
- A1.13 Consistent with the method set out above, the required reduction is calculated in two steps:
- 1.13.1 the real reduction ('Y') required to move from the start point to the end point is calculated. This calculation gives a Y-value of -2.90%.
  - 1.13.2 a geometric conversion is then applied to the real Y-value. The geometric conversion factor is 2.5%<sup>4</sup>, which gives an X-value of **3.0%** (rounded to 1 decimal place). We use this X value in an RPI-X formula to calculate the nominal charge ceiling for the final year of the charge control.

### Revised figures

- A1.14 The real charges (in 2008/09 prices) resulting from the Determination and the Tribunal's directions are set out in the third row of Table 2 below.
- A1.15 The revised figures (nominal charges or the value of 'X') resulting from the two calculations described above can be seen in the final row of Table 2. It is these figures which are reflected in the revisions to Condition M3 contained in the operative part of this document. As the condition is being revised part way through the 2012/13 charge control year, only the figures for 2012/13, 2013/14 and 2014/15 are reflected in the revisions.

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<sup>4</sup> Consistent with the approach taken to the geometric conversion factor in the MCT Statement, we have used forecast inflation of 2.5% for all years after 2011/12. For the final year X-value, no averaging over charge control years is required to derive the geometric conversion factor, since we are dealing with only a single year's change.

**Table 2 – Comparison of charge ceilings**

	2011/12	2012/13	2013/14	2014/15
<b><i>Real charges (ppm, 2008/09 prices)</i></b>				
MCT Statement (March 2011)	2.664	1.698	1.083	0.690
Modification (October 2011)	2.693	1.735	1.118	0.720
Tribunal's directions (May 2012)	2.293	1.258	0.690	0.670
<b><i>Nominal charges (ppm) / value of 'X'<sup>5</sup></i></b>				
Modification (October 2011)	3.015 <sup>6</sup>	2.053	36.7%	36.7%
Tribunal's directions (May 2012)	2.577	<b>1.500</b>	<b>46.6%</b>	<b>3.0%</b>

## Revisions to SMP Condition

- A1.16 The revised figures resulting from the calculations described above are implemented by means of an amended definition of “controlling percentage” and amendments to Condition M3.4.
- A1.17 As the Tribunal's judgment has been issued part-way through the 2012/13 charge control year (which commenced on 1 April 2012), it is necessary also to amend the definition of “relevant period” in order to split the 2012/13 charge control year into two periods (the “third relevant period” and the “fourth relevant period”). The revised nominal charge ceiling for 2012/13 (1.500ppm) applies for the fourth relevant period from the date the revisions to the charge control take effect until 31 March 2013.

## Notice period

- A1.18 In accordance with the Determination, Ofcom has considered what would be an appropriate period of notice to allow before the adjustments to the charge control take effect.
- A1.19 Ofcom's view is that observation of the typical 28 day regulatory notice period would not be appropriate in the circumstances of this case. In particular, following the publication of the Determination, the mobile operators and their counterparties have been on notice for several months that an adjustment is liable to be made to the level of the charge control, and the potential parameters of that adjustment.

<sup>5</sup> Nominal charges can only be calculated when the change in RPI for the immediately preceding calendar year becomes available. Nominal charges are therefore only stated for 2011/12 and 2012/13. For subsequent charge control years, the nominal charge is calculated by applying an RPI-X formula to the nominal charge applicable in the previous charge control year. Since the nominal charge ceiling in ppm terms cannot be given for 2013/14 and 2014/15, the value of 'X' in the RPI-X formula is therefore shown in the table for these charge control years.

<sup>6</sup> A nominal charge ceiling of 2.984 applied from 1 April 2011 until the date on which the Modification took effect.

- A1.20 In a letter to the Tribunal of 2 March 2012 (referred to at paragraph 330 of the Tribunal's judgment), Ofcom stated its intention to notify and publish the required modifications to the SMP Conditions such that the adjustment to the charge control would take effect without delay following the date on which the Tribunal issued judgment disposing of the appeals. The Tribunal has not directed Ofcom to do otherwise on the disposal of the appeals, and we are therefore adopting this approach.
- A1.21 To the extent that compliance with the revisions to Condition M3, set out in the operative part of this document, prevents the mobile operators from complying with SMP Condition M4.3 (the obligation to provide 28 days' advance notice of amendments to charges), then Ofcom will not take any enforcement action in this instance in relation to the failure to provide such notice.