Mobile call termination: A simpler pricing rule

Supplemental consultation

Publication date: 16 Nov 2010

Closing Date for Responses: 14 Dec 2010

Contents

Section 1

Executive summary

1.1 This consultation supplements our consultation published on 1 April 2010 (the 'April 2010 consultation')[1] as part of our review of the markets in which mobile call termination on individual mobile networks is supplied in the UK.[2]

1.2 We are seeking comments from stakeholders on a change to our preferred approach for setting a pricing rule. This change is in response to comments from stakeholders to our April 2010 consultation and following further discussions with industry at a workshop to discuss our proposals for an appropriate pricing rule held on 12 October 2010.

1.3 We are now proposing, as our preferred approach, to set a *maximum* ceiling price rule (currently, an *average* price rule applies). Our reasons for this change are set out in section 2 of this consultation. In summary, given stakeholders' comments, we now believe that a simpler rule which addresses our concerns over previously frequent and significant changes to MTRs (so-called 'flip-flopping') is more appropriate.

1.4 This proposed change affects the charge control condition we proposed to impose on Everything Everywhere (previously T-Mobile and Orange), Vodafone, O2 and H3G. We are therefore seeking comments on the proposals and corresponding minor amendments to our proposed 'significant market power' (SMP) conditions in this consultation (see annex 5).

1.5 As this consultation is an extension of the broader April 2010 consultation, follows an industry workshop where the issues were discussed and only covers a relatively small change in the approach set out in our April 2010 consultation, we only intend to consult on these issues for a period of 4 weeks. As such we are seeking submissions from stakeholders on the issues set out in this document by **14 December 2010**.

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[1] http://stakeholders.ofcom.org.uk/consultations/wmctr/

[2] When fixed and mobile providers offer their customers the ability to call UK mobile numbers, they pay mobile communications providers a wholesale charge to complete those calls. The rates that providers pay are called 'mobile call termination' (MCT) charges or more commonly 'mobile termination rates' (MTRs).

Section 2

A simpler pricing rule

Introduction

2.1 Under the current charge control, the four national MCPs are able to change their MTRs as often as they wish; provided that they ensure their *average* charge does not exceed the limit set by regulation.[3] They may also set different MTRs at different times (for example, for day, evening, weekend rates or any other charging period - termed 'time of day flexibility').

2.2 Although this flexibility was originally conceived as a tool to manage network traffic, some providers have used this flexibility to 'flip-flop' their rates. 'Flip-flopping' refers to the practice whereby some national MCPs have made frequent and significant changes to their MTRs.

2.3 Flip-flopping works by exploiting the difference in the number of weekends in each month between the prior year and the current year, because the calculation used to monitor compliance with the charge control uses prior year's volumes. By identifying the months in the current year where the number of weekends differs from the same months in the prior year, prices can be structured to maximise revenues.

2.4 When the number of weekends in a particular month increases from four to five, for example, between the prior year and the current year, a MCP can increase its prices at the weekend and decrease prices in the day and evening. Because the prior year had a lower number of weekends than the current year, the higher price is given a lower weighting for the purpose of calculating compliance. However, in the current year, it gives the provider an extra weekend of revenue at the high price. If the opposite happens in a month and the number of weekends decreases from five to four, the provider can price high in the day and evening, and low at the weekends. If the effect reverses month-on-month, then prices are flipped. In our April 2010 consultation we noted that in some cases we had seen MTRs change from a range of around 12p to 15p at the weekend in one month, to 2p to 5p in the next month.

2.5 Flip-flopping is undesirable because it undermines the core purpose of the MCT charge control (by securing up to an additional 5% revenue under the charge control than envisaged by us when we set the original control (in March 2007). In practice, this can secure some MCPs additional tens of millions of pounds in revenue. Not only does the practice of flip-flopping allow MCPs to gain extra revenue, frequent and significant changes in time of day rates increase the risk for originating providers and also raise their costs, in a way that is not susceptible to competitive pressure (that is, the source of the ability to flip-flop is related to the underlying position of significant market power (SMP) in call termination). (A more detailed explanation of these issues is provided in our April 2010 consultation).[4]

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[3] The current pricing rule for mobile call termination is as set in pages 396 to 408 in Annex 20 of our March 2007 Mobile Call Termination Statement (http://stakeholders.ofcom.org.uk/binaries/consultations/mobile_call_term/statement/statement.pdf)

[4] See, for example, paragraphs 9.120 to 9.126 of the April 2010 consultation http://stakeholders.ofcom.org.uk/binaries/consultations/wmctr/summary/wmvct_consultation.pdf

2.6 Several respondents to our initial consultation[5] in May 2009 raised such concerns.[6] Frequent and significant changes in wholesale mobile termination rates (MTRs) will impact on purchasers of MCT (and ultimately consumers), for example, some purchasers of MCT may need to set higher retail prices to their customers to lessen the impact of these frequent changes to mitigate the risk of setting retail prices significantly below the wholesale rates.

2.7 Even if new rates were not directly passed through to consumers in the form of high retail prices at the time they happen, retail customers are still likely to lose out in the long run from higher overall rates. If originating providers do not pass through any kind of price increase (or allow a premium in retail tariffs to cover future expected increases) then they will be worse off.[7] In practice, this means that they are likely to recover those additional costs in some way that is ultimately borne by consumers.

2.8 Reflecting these concerns, in the April 2010 consultation we consulted on four options to prevent flip-flopping. We suggested that our preferred option to prevent flip-flopping was to retain the average price rule which applies under the current control, but to limit the number and size of price changes each MCP could adopt.

2.9 Following further discussions with stakeholders and having reviewed responses to the April 2010 consultation, we are now proposing two new options which are variants of two of the original options. We discussed these options with industry on 12 October 2010 in an industry workshop. Of these two new options, we believe that there is one (setting a maximum price) that is preferred by both Ofcom and stakeholders. It deals with the problems surrounding flip-flopping in what we believe to be the least intrusive way possible and still retains pricing flexibility. We are now seeking views on these options and on our preference for which one is best.

2.10 In the April 2010 consultation we set out four options for amending the charge control formula during the period covered by this market review:[8]

- Option 1 – adopt a formula similar to the 2007 control

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[5] See: http://stakeholders.ofcom.org.uk/binaries/consultations/mobilecallterm/summary/mobile_call_term.pdf

[6] For example, in Colt's response to the preliminary consultation (see pages 4 and 5 of COLTs response at http://www.ofcom.org.uk/consult/condocs/mobilecallterm/responses/COLT.pdf), it states that "*it is impossible for most CPs to alter their retail pricing to reflect these changes. It is a regulatory requirement that customers are given a minimum of one month's notice for price changes. In the corporate market many large customers are on fixed-price, fixed-term contracts which make price changes impossible. In any case such monthly price changes would be onerous and confusing for customers*". In its response to the same consultation C&W also supports a change and states that "*frequent price changes make it difficult for CPs to assess whether the MCP is complying with the charge control and there is potential for the price changes to result in a detriment of some operators over others depending on the particular operator's traffic profile. In addition frequent price changes place CPs under an administrative burden as these are reflected in charges to customers. This inevitably ripples through to retail pricing and the customer can have no hope of keeping up with the applicable charge for their calls*." (see Page 3 of C&W's response at: http://www.ofcom.org.uk/consult/condocs/mobilecallterm/responses/CableWireless.pdf

[7] We have also received informal representations from potential new entrants that the frequent and radical price changes are a particular problem. As they cannot be certain of what the MTRs will be from one month to the next, it is difficult for potential new entrants to estimate their outgoing payments. One potential new entrant, in informal discussions with Ofcom, highlighted that this is particularly problematic in the context of trying to obtain funding.

[8] Paragraph 9.128- 91.60 http://stakeholders.ofcom.org.uk/binaries/consultations/wmctr/summary/wmvct_consultation.pdf

- Option 2 – restrict the frequency and size of MTR changes
- Option 3 – impose a constant time of day rate ratio
- Option 4 – impose a single, constant, flat MTR for each whole year of the control

2.11 Options 2, 3 and 4 each aimed to address flip-flopping and we considered each against whether it:

2.11.1 targeted the specific problems identified, which are the disruption to other providers (resulting from frequent and radical MTR changes) and the harm to consumers (paying excessive prices for a service not subject to competition)? and

2.11.2 retained sufficient flexibility to vary MTRs by time of day to encourage efficient use of the network?

2.12 Having reviewed each option, the preference we expressed in the April 2010 consultation was for Option 2, and we sought comments from stakeholders on this approach.

Responses to the April 2010 consultation

2.13 Responses to the April 2010 consultation raised some consistent themes regarding our approach to flip-flopping.

2.14 In general responses to our proposals considered that preventing flip-flopping was a good idea. The majority of respondents, including MCPs, agreed that regulation should prevent frequent and significant changes in MTRs – and agreed with our assessment that flip-flopping harmed the interests of other providers and, indirectly, consumers.

2.15 Submissions also provided more detail on the way in which flip-flopping disrupted the operation of the market. For example, UCKTA commented that "*left unchecked this practice would allow MCPs to continue to force purchasers of MCT to pay more, in aggregate, than the rates intended to be set as an upper limit. In addition, this practice also forces competing operators to incur extra costs, as the MTRs are frequently changed by significant amounts, requiring price notifications to be prepared and distributed to customers, in compliance with contractual obligations."* [9] Talk Talk commented that '*the uncertainty caused by flip-flopping reduces and delays our ability to pass through any mobile termination reductions to our customers who will be disadvantaged as a result.*'[10]

2.16 A number of fixed and smaller mobile providers (including BT, C&W, Mundio Mobile and Talk Talk) also commented that constant and unpredictable MTR changes placed an administrative burden on them and made commercial planning more difficult. In particular, C&W say explicitly that such frequent MTR changes "*place[s] an administrative burden on operators to keep changing prices*".

2.17 H3G commented that setting different MTRs by charging period no longer sends out relevant pricing signals for mobile-to-mobile calls as retail packages rarely

[9] http://stakeholders.ofcom.org.uk/binaries/consultations/wmctr/responses/UKCTA.pdf
[10] http://stakeholders.ofcom.org.uk/binaries/consultations/wmctr/responses/TalkTalk_Group.pdf

differentiate charges according to time of the day[11]. Colt argued that the practice of flip-flopping itself demonstrates the lack of any commercial value in providing this flexibility.[12]

2.18 Of the national MCPs, both H3G and Everything Everywhere favoured options that did not allow any time of day flexibility. Under the current control O2 has consistently been charging a flat-rate. Only one respondent, Vodafone, commented that it considered time of day flexibility to still be valuable to encourage efficient network use, "*the need for flexibility is that it does allow the operators the possibility of optimising the use of their network through encouraging traffic at low usage times. However in order for wholesale rates to have any real impact on traffic mix, there must be some form of predictable continuity in order for originating operators to be able to react in a way that might encourage traffic at times of low usage.*"[13]

2.19 Many of the respondents including H3G, also commented that our preferred option in the April 2010 consultation (option 2) was overly prescriptive and complex, and a simpler rule, along the lines of option 4, would be more appropriate.

2.20 In light of these responses, and following further discussion with industry at a stakeholder workshop on 12 October 2010, we have dismissed options 1 and 3, and have refined options 2 and 4 for the charge control formula set out in our April 2010 consultation on which now invite comments. We have also changed our preferred approach, as set out below.

Revised options for the charge control formula

2.21 Consistent with what we said in the April 2010 consultation (see, paragraphs 9.110 to 9.126) we continue to believe that we should adopt a rule that prevents, or severely restricts the worst effects, of flip-flopping in the future.

2.22 Option 1 set out in the April 2010 consultation represents the status-quo, meaning that each of the national MCPs would still be free to vary their MTRs as often as they wished, provided the *average* charge did not exceed the limit set by regulation. As such, they could continue to vary MTRs frequently and significantly. We continue to think that this option is not a viable option, as it would not address the issue of flip-flopping, and therefore would not address the consumer detriments we believe are caused by the practice of flip-flopping.

2.23 Similarly, we do not consider that option 3 (imposing a constant time of day ratio) would be a particularly attractive approach. This option would restrict frequent and radical rate changes but would be inflexible to any changes in traffic profiles or behaviour outside the MCPs control. A fuller assessment of these options is provided in the April 2010 consultation (see paragraphs 9.129 to 9.132 and 9.145 to 9.149).

2.24 We believe that option 2 or 4, with some additional revisions to reflect input from stakeholders, remain the most appropriate options. This consultation therefore seeks stakeholders views on these two revised options, they are:

- Option 5 – to allow full time of day flexibility, but limit the number of changes to one during each year (a variation on our previous option 2); and

[11] http://stakeholders.ofcom.org.uk/binaries/consultations/wmctr/responses/H3G.pdf
[12] http://stakeholders.ofcom.org.uk/binaries/consultations/wmctr/responses/Colt.pdf
[13] http://stakeholders.ofcom.org.uk/binaries/consultations/wmctr/responses/Vodafone.pdf

- Option 6 - to set a price ceiling on MTRs, allowing flexibility of charging so long as any charges set do not exceed that ceiling (a variation on our previous option 4)

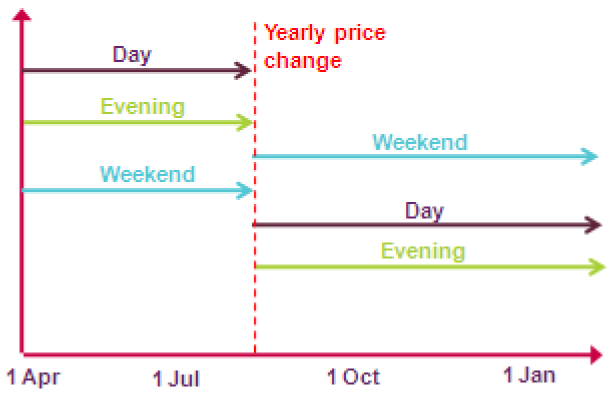
2.25 We presented both of these revised options at the industry workshop on 12 October 2010. Below we set out further details of both options and set out which of these is our preferred option.

Option 5 - Set a maximum average charge with only one price change during each year

2.26 This option is a variant of the previous option 2 set out in the April 2010 consultation. Option 2 was similar to the current control in that it was an average charge allowing MCPs the flexibility to vary charges over the year. However it placed restrictions on both the frequency and size of any changes. Changes would only be able to occur on the first day of each quarter, and would be restricted to a maximum increase between each time of day period of 20%.

2.27 This revised option (option 5), only allows each MCPs to make a single rate change during the year (at the start of any month during that year), but places no restriction on the size of the rate change. By restricting the number of changes to one in each relevant year the ‘extra’ termination revenue obtained by flip-flopping is greatly diminished.

Figure 1 Example of pricing by time of day



How the compliance calculation would work

2.28 Compliance would be assessed on the average of the rates levied by each of the MCPs (i.e. across time-of-day charges) for terminating voice calls, weighted by the relative call volumes in the previous year. This average call termination charge must not exceed the charge with which the operator is required to comply, i.e. the maximum average charge set under the SMP condition. This option therefore follows broadly the same structure as the current control.

2.29 This option would reduce the frequency of any substantial MTR changes, whilst retaining time-of-day flexibility. If time-of-day pricing were being used for its intended purpose, we would not expect the structure of MTRs to change significantly or frequently within a short period of time (since otherwise it would not provide consistent and predictable price signals). However, in order to prevent flip-flopping this option adds further restrictions to the current control – i.e. the scope for only a single charge change within the year, and is more complex than option 6.

2.30 In order to assess compliance, this option requires MCPs to provide prior year call volumes to Ofcom[14] and therefore has some administrative costs to the national MCPs.

Option 6 - Set a price ceiling

2.31 This option is similar to option 4 from the April 2010 consultation where we proposed a single flat rate (though rates could be below this single flat rate). However under this approach, MTRs must not exceed a single, constant, maximum charge – a price ceiling - set for each whole year of the control.

2.32 There are two main differences between this option (option 6) and the approach set out as option 4 in the April 2010 consultation. Previously we proposed:

- to restrict the number of changes in a year to one (on 1 April); and
- to restrict the ability to vary charges by time of day.

2.33 Both Vodafone and Everything Everywhere commented that it was not necessary for this type of price rule to restrict MCPs to just one change per year on 1 April; any number of price changes could be made without reducing the effectiveness of the rule.

2.34 Under this revised option, there would be a single maximum charge applying to those MCPs on whom we impose a charge control. However they would be free to set different time of day rates and change the rate without restriction provided the charge ceiling is not exceeded. Figures 2 and 3 below show stylised examples of the pricing strategies MCPs could adopt under this revised option.

[14] The use of prior year call volumes (since the current year volumes are, by definition, not known at the time a price is set) is one element that enables flip-flopping.

Figure 2 Example of a single flat rate with multiple changes in the year

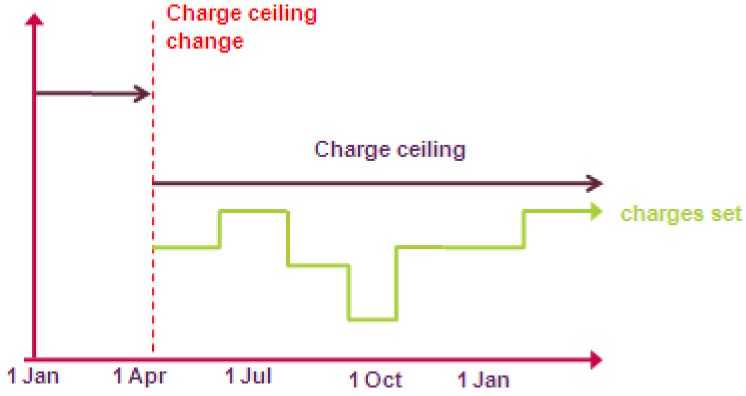
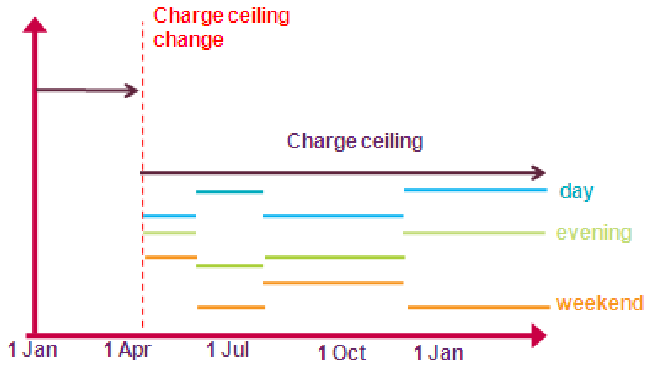


Figure 3 Example of time of day rates with multiple changes in the year



How the compliance calculation would work

2.35 Under this option our final statement would set the maximum charge for the first year and specify a formula that will determine the maximum charge for each subsequent year.[15]

2.36 Since MTRs must not exceed the maximum charge ceiling, unlike previous charge controls, there would be no need for any 'compliance calculation'. In particular, MCPs would not need to provide volumes to Ofcom. Our compliance monitoring would need only to ensure that the MTR was set at or below the maximum charge ceiling. The cost of compliance for the MCPs would also be negligible, as no calculation would be required in setting rates to check that they were compliant.

[15] The glide path and its implementation, which we will determine in our final statement for this market review, will set the level of the charge cap. The target for efficient unit costs will determine the ceiling at the end of the glide path. The MCT cost model is based on end of year costs. When estimated unit costs are falling for each year modelled, the unit cost at the end of the year will be lower than the unit cost at the start of the year. When unit costs are increasing for each year modelled, the reverse will be true. We wish to avoid being in a situation where due to the glide-path mechanism we force the MTRs below costs in the final year of the glide-path. As such, when selecting the final cost based target, we propose to use the unit cost estimate for the year prior to the end of the glide-path when charges are decreasing and the unit cost estimate for the year of the end of the glide-path when charges are increasing. In the April 2010 consultation version of the MCT model, the unit costs are falling over each year modelled and so we would set the end of glide-path target charge on the prior year's unit cost estimate.

Our preferred option – option 6

2.37 As in our April 2010 consultation, we have considered each option against whether it:

2.37.1 targets the specific problems identified, which are the disruption to other providers (resulting from frequent and radical MTR changes) and the harm to consumers (paying excessive prices for a service not subject to competition)? And

2.37.2 retains sufficient flexibility to vary MTRs by time of day to encourage efficient use of the network?

2.38 Having taken account of stakeholder responses to our previously preferred option (set out in our April 2010 consultation), feedback from our industry stakeholder event, and having given further consideration to the options, our preference is now for a maximum charge ceiling for MCT, applicable for the entire charge control year (option 6).

2.39 We believe that this is a proportionate remedy. It has the benefit of simplicity and it achieves the objective of severely restricting flip-flopping and preventing it at rates above the ceiling, thereby removing concerns over the consumer detriment that we believe occurs through the practice of flip-flopping. In addition, this revised option allows MCPs some flexibility in how they set their MTRs, removing restrictions on the frequency of price changes, maintaining the ability for MCPs to set different time-of-day MTRs, whilst also providing certainty to purchasers of MCT over the maximum level of MTR allowed. To the extent that pricing flexibility remains useful for MCPs wanting to affect usage of their network, this option allows some flexibility to do so. Finally, because of its simplicity it also reduces the cost of compliance, therefore reducing the likelihood of future regulatory disputes.

2.40 While the maximum charge ceiling option restricts MCPs' time of day pricing flexibility compared to the current control, consistent with stakeholder responses we believe that this greater level of flexibility is no longer required for incentivising efficient use of the network.

2.41 The feedback from stakeholders from the April 2010 consultation and the industry stakeholder event was that the majority of stakeholders favoured a simple pricing rule, that allowed predictability of pricing, whilst still preventing flip-flopping. H3G, Colt and Talk Talk all expressed a preference for option 4 (which is similar to our preferred option 6) in response to the April 2010 consultation and those responses regarding the alternative options were that these options either did not meet the objective of preventing flip-flopping or they were overly prescriptive and complex.

2.42 Paragraphs 2.43 to 2.55 below set out the legal tests relevant to this proposed change and Annex 5 shows how Condition M3 of the SMP Conditions in schedule 2 of annex 7 of the April 2010 consultation is amended to reflect changes to our preferred option.

Legal tests

2.43 At Annex 7 to the consultation document published on 1 April 2010, we published a notification in accordance with our duty under section 48(2) of the Communications Act 2003, stating that we were proposing to set SMP conditions, setting out the effect of those conditions, and giving our reasons for making the proposal. For the reasons set out above, in response to consultation feedback in writing and at our stakeholder event on this issue we are now continuing to consult on this aspect and attach a further draft of Condition M3 at Annex 5 to this document. We invite further representations in relation to the modifications set out in this consultation.

2.44 Section 87(1) of the Communications Act (the Act) provides that, where Ofcom has made a determination that a person has SMP in the market reviewed, it must set such SMP conditions as it considers appropriate and as are authorised in the Act. In the April 2010 consultation we set out (in Annex 7) those MCPs that we considered held a position of SMP in the MCT market.

2.45 The Act (sections 45-50 and 87-92) sets out the regulatory obligations that we can impose if we find that any undertaking has SMP. In the April 2010 consultation we set out a number of conditions to apply to MCPs holding a position of SMP in MCT. This consultation makes amendments to Condition M3 (Control of fixed-to-mobile and Mobile-to-Mobile MCT call charges) set out in the April 2010 consultation.

2.46 The April 2010 consultation sets out the legal tests relevant to applying SMP conditions, including our general duties under Sections 3 and 4 of the Act.

2.47 Section 87(1) of the Act requires that each SMP condition must also satisfy the tests set out in section 47 of the Act, namely that each condition must be:

- objectively justifiable in relation to the networks, services, facilities, apparatus or directories to which it relates;
- not such as to discriminate unduly against particular persons or against a particular description of persons;
- proportionate to what the condition is intended to achieve; and
- in relation to what it is intended to achieve, transparent.

2.48 We think that the amended condition set out below (and in annex 5) satisfies the relevant requirements specified in the Act and relevant European Directives. In the following paragraphs, we set out the revised condition M3, the aims of the amended Condition M3 and relate these to the requirements of Section 47 of the Act.

Suggested possible amendment to Condition M3 - Control of fixed-to-mobile and mobile-to-mobile MCT Call charges

2.49 The suggested new Condition M3 is set out in full below.

Suggested new maximum price ceiling mechanism

Condition M3 – Control of termination charges

M3.1 The dominant provider shall ensure that for each Call on any day, during any relevant year, the call termination charge does not exceed the charge ceiling.

M3.2 The charge ceiling is:

(a) for any Call on a day in the First Relevant Year, [….] pence per minute;

(b) for any Call on a day in the Second Relevant year, Third Relevant Year or Fourth Relevant Year:

a sum equal to the charge ceiling, expressed in pence per minute, in the relevant year preceding the relevant year in which the Call was made, multiplied by the sum of 100% and also multiplied by the controlling percentage for the relevant year in which the Call was made (without rounding up or down) and expressed as being pence per minute, which total is then rounded to three decimal places (and expressed as being pence per minute).

M3.3 The dominant provider shall not make any call termination charge for:

(a) a Call which terminates on a recorded announcement provided by the dominant provider informing the caller of an inability to complete that Call so as to establish a two-way path where the mobile handset used by the called party is switched off, or rings and remains unanswered, or where coverage is not available from the dominant provider's public electronic communications network; and

(b) an unanswered Call which is diverted in respect of the period before that Call is answered.

M3.4 Without prejudice to Ofcom's statutory information gathering powers, the dominant provider shall provide to Ofcom in writing any information reasonably required by Ofcom to demonstrate compliance with this SMP condition at any time during the Relevant Year upon reasonable notice.

M3.5 The dominant provider shall comply with any direction Ofcom may make from time to time under this SMP condition.

For the purposes of SMP condition M3 only:

"**dominant provider**" means [H3G], [02], [Vodafone] and [Everything Everywhere].

2.50 Annex 5 shows the revisions to Schedule 2 of Annex 7 of the April 2010 consultation reflecting the changes to condition M3 discussed in this document. For the purposes of clarity and transparency, annex 5 includes the whole of schedule 2 of annex 7 as it appeared in the April 2010 consultation.

2.51 For the reasons set out in Sections 7 and 9 of the April 2010 consultation, the suggested new condition M3 only applies to the four national MCPs and its purpose is to control the charge which any of these MCPs may set in respect of MCT (including calls originated on both fixed and mobile networks). The charge controls would be imposed for a period of four years from 1 April 2011. We do not propose to change these aspects of Condition M3 in this consultation.

2.52 The suggested new condition M3.1 requires the dominant MCP to ensure that, for each Call during any relevant year, the call termination charge does not exceed the maximum charge. Condition M3.2 sets the maximum charge in pence per minute for the first relevant year (condition M3.2(a)) and for future relevant years (condition M3.2(b)).

2.53 Condition M3.3 identifies calls for which the dominant provider should not make any call termination charge. Condition M3.4 sets out information that the dominant provider shall provide to Ofcom necessary for monitoring compliance with this SMP condition. Condition M3.5 requires the dominant provider to comply with any direction that Ofcom may make from time to time under this SMP condition.

2.54 This mechanism is likely to meet the relevant legal tests set out in Section 47 of the Act in that it is justifiable, non-discriminatory, proportionate and transparent. This consultation looks not at the level of the price control but at the mechanism for its operation.

2.55 As described in our consultation a price control mechanism is, we believe, appropriate when measured against the legal tests described in paragraph 2.46 to 2.47 above. With that in mind it does seem to Ofcom that this is the most appropriate mechanism, because it is clear and simple, and therefore transparent. Is the least intrusive option of those available because it retains pricing flexibility below the ceiling, and therefore we believe is likely to be the most proportionate option available. It is a small change in effect as it moves from a maximum average charge to a price ceiling. It is objectively justifiable because it is likely to remove the problematic effects of the previous rule. It is non-discriminatory as it applies to each of the four national MCPs, and further reduces discriminatory effects for other companies which had to cope with fluctuations in charges to them. It is also targeted at the problem, and will deliver benefits to consumers.

Question 2.1: Is a maximum price ceiling rule the best mechanism to address the problem of flip-flopping?

Compliance

2.56 We also propose a number of minor amendments to make compliance as straightforward as possible.

Ofcom to publish the nominal cap prior to the start of each control year

2.57 In the SMP condition, we can set the nominal maximum charge for the first relevant year directly (that is, in the text of the SMP condition). For the remaining three years of the charge control, the maximum charge would be calculated using a formula, with the nominal charge able to be calculated once the relevant inflation data is published (i.e. the relevant inflation series being based on RPI for the year ending 31 December before the start of the new charge control year).

2.58 In the interests of transparency and certainty, we would publish our assessment of the maximum charge applying during the second, third and fourth relevant years of the charge control when the inflation information became available.

2.59 We anticipate this would be useful, particularly to providers who purchase MCT. The underlying source of the obligation on regulated MCPs would remain that set out in the SMP condition, and not the number published by Ofcom. In the event of any inconsistency, it would be the formula that applied.

Rounding

2.60 Currently MCPs set MTRs to either three or four decimal places. It is in the interests of all parties, and ultimately, consumers, that there is a common practice to ensure consistency amongst different interconnecting operators.

2.61 Recognising that not all billing systems can accommodate calculations to four decimal places, we propose to set the maximum charge in pence per minute to three decimal places.

2.62 To demonstrate compliance, MCPs would need to ensure that their charges are also set to three decimal places and do not exceed the maximum charge.

Question 2.2: Do you think the maximum charge should be stated to three decimal places?

Demonstrating and monitoring compliance

2.63 In light of our preferred option for a simpler approach, there are some consequential changes to the way in which we propose that compliance should be demonstrated and monitored under our preferred approach.

2.64 Setting a maximum charge does not require consideration of how many calls have been made (call volumes) to assess compliance. The only information required is notification of each charge (or charges) set by the MCPs over the Relevant Year.

2.65 The information required to demonstrate compliance is set out in the draft SMP conditions in Annex 5.

Conclusion

2.66 On the basis of the discussion set out above we are now seeking stakeholders' views, particularly on options 5 and 6, and on our preference for option 6.

2.67 As this consultation is an extension of the broader April 2010 consultation, follows an industry workshop where the issues were discussed and only covers a relatively small change in the approach set out in our April 2010 consultation, we only intend to consult on these issues for a period of 4 weeks. As such we are seeking submissions from stakeholders on the issues set out in this document by **14 December 2010**.

Annex 1

Responding to this consultation

How to respond

A1.1 Ofcom invites written views and comments on the issues raised in this document, to be made **by 5pm on 14 December 2010**.

A1.2 Ofcom strongly prefers to receive responses using the online web form at http://stakeholders.ofcom.org.uk/consultations/mtr, as this helps us to process the responses quickly and efficiently. We would also be grateful if you could assist us by completing a response cover sheet (see Annex 3), to indicate whether or not there are confidentiality issues. This response coversheet is incorporated into the online web form questionnaire.

A1.3 For larger consultation responses - particularly those with supporting charts, tables or other data - please email MCT.Review@ofcom.org.uk attaching your response in Microsoft Word format, together with a consultation response coversheet.

A1.4 Responses may alternatively be posted or faxed to the address below, marked with the title of the consultation.

Paul Jacobus
4th Floor
Competition Group
Riverside House
2A Southwark Bridge Road
London SE1 9HA

A1.5 Note that we do not need a hard copy in addition to an electronic version. Ofcom will acknowledge receipt of responses if they are submitted using the online web form but not otherwise.

A1.6 It would be helpful if your response could include direct answers to the questions asked in this document, which are listed together at Annex 4. It would also help if you can explain why you hold your views and how Ofcom's proposals would impact on you.

Further information

A1.7 If you want to discuss the issues and questions raised in this consultation, or need advice on the appropriate form of response, please contact Paul Jacobus on 020 7981 3574.

Confidentiality

A1.8 We believe it is important for everyone interested in an issue to see the views expressed by consultation respondents. We will therefore usually publish all responses on our website, www.ofcom.org.uk, ideally on receipt. If you think your response should be kept confidential, can you please specify what part or whether all of your response should be kept confidential, and specify why. Please also place such parts in a separate annex.

A1.9 If someone asks us to keep part or all of a response confidential, we will treat this request seriously and will try to respect this. But sometimes we will need to publish all responses, including those that are marked as confidential, in order to meet legal obligations.

A1.10 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use. Ofcom's approach on intellectual property rights is explained further on its website at http://www.ofcom.org.uk/about/accoun/disclaimer/

Next steps

A1.11 Following the end of the consultation period, Ofcom intends to publish a statement in the first quarter 2011.

A1.12 Please note that you can register to receive free mail Updates alerting you to the publications of relevant Ofcom documents. For more details please see: http://www.ofcom.org.uk/static/subscribe/select_list.htm

Ofcom's consultation processes

A1.13 Ofcom seeks to ensure that responding to a consultation is easy as possible. For more information please see our consultation principles in Annex 2.

A1.14 If you have any comments or suggestions on how Ofcom conducts its consultations, please call our consultation helpdesk on 020 7981 3003 or e-mail us at consult@ofcom.org.uk . We would particularly welcome thoughts on how Ofcom could more effectively seek the views of those groups or individuals, such as small businesses or particular types of residential consumers, who are less likely to give their opinions through a formal consultation.

A1.15 If you would like to discuss these issues or Ofcom's consultation processes more generally you can alternatively contact Vicki Nash, Director Scotland, who is Ofcom's consultation champion:

Vicki Nash
Ofcom
Sutherland House
149 St. Vincent Street
Glasgow G2 5NW

Tel: 0141 229 7401
Fax: 0141 229 7433

Email vicki.nash@ofcom.org.uk

Annex 2

Ofcom's consultation principles

A2.1 Ofcom has published the following seven principles that it will follow for each public written consultation:

Before the consultation

A2.2 Where possible, we will hold informal talks with people and organisations before announcing a big consultation to find out whether we are thinking in the right direction. If we do not have enough time to do this, we will hold an open meeting to explain our proposals shortly after announcing the consultation.

During the consultation

A2.3 We will be clear about who we are consulting, why, on what questions and for how long.

A2.4 We will make the consultation document as short and simple as possible with a summary of no more than two pages. We will try to make it as easy as possible to give us a written response. If the consultation is complicated, we may provide a shortened Plain English Guide for smaller organisations or individuals who would otherwise not be able to spare the time to share their views.

A2.5 We will consult for up to 10 weeks depending on the potential impact of our proposals. In this case, for the reasons set out in paragraph 2.67 above, we only propose to consult for four weeks.

A2.6 A person within Ofcom will be in charge of making sure we follow our own guidelines and reach out to the largest number of people and organisations interested in the outcome of our decisions. Ofcom's 'Consultation Champion' will also be the main person to contact with views on the way we run our consultations.

A2.7 If we are not able to follow one of these principles, we will explain why.

After the consultation

A2.8 We think it is important for everyone interested in an issue to see the views of others during a consultation. We would usually publish all the responses we have received on our website. In our statement, we will give reasons for our decisions and will give an account of how the views of those concerned helped shape those decisions.

Annex 3

Consultation response cover sheet

A3.1 In the interests of transparency and good regulatory practice, we will publish all consultation responses in full on our website, www.ofcom.org.uk.

A3.2 We have produced a coversheet for responses (see below) and would be very grateful if you could send one with your response (this is incorporated into the online web form if you respond in this way). This will speed up our processing of responses, and help to maintain confidentiality where appropriate.

A3.3 The quality of consultation can be enhanced by publishing responses before the consultation period closes. In particular, this can help those individuals and organisations with limited resources or familiarity with the issues to respond in a more informed way. Therefore Ofcom would encourage respondents to complete their coversheet in a way that allows Ofcom to publish their responses upon receipt, rather than waiting until the consultation period has ended.

A3.4 We strongly prefer to receive responses via the online web form which incorporates the coversheet. If you are responding via email, post or fax you can download an electronic copy of this coversheet in Word or RTF format from the 'Consultations' section of our website at www.ofcom.org.uk/consult/.

A3.5 Please put any parts of your response you consider should be kept confidential in a separate annex to your response and include your reasons why this part of your response should not be published. This can include information such as your personal background and experience. If you want your name, address, other contact details, or job title to remain confidential, please provide them in your cover sheet only, so that we don't have to edit your response.

Cover sheet for response to an Ofcom consultation

BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

CONFIDENTIALITY

Please tick below what part of your response you consider is confidential, giving your reasons why

Nothing	☐	Name/contact details/job title	☐
Whole response	☐	Organisation	☐
Part of the response	☐	If there is no separate annex, which parts?	

If you want part of your response, your name or your organisation not to be published, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response that Ofcom can publish. However, in supplying this response, I understand that Ofcom may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations. If I have sent my response by email, Ofcom can disregard any standard e-mail text about not disclosing email contents and attachments.

Ofcom seeks to publish responses on receipt. If your response is non-confidential (in whole or in part), and you would prefer us to publish your response only once the consultation has ended, please tick here. ☐

Name Signed (if hard copy)

Annex 4

Consultation questions

consultation questions

Question 2.1: Is a maximum price ceiling rule the best mechanism to address the problem of flip-flopping?

Question 2.2: Do you think the maximum charge should be stated to three decimal places?

Annex 5

Revisions to Schedule 2 of Annex 7 of the April 2010 consultation reflecting changes to SMP condition M3

This annex reproduces schedule 2 to the Notification under sections 4(2) and 80 of the Communication Act 2003 included as annex 7 of the April 2010 consultation. As such it includes all of the SMP conditions proposed in the April 2010 consultation, though only SMP condition M3 has been amended. Were necessary, following the amendments made to condition M3, the revisions made to part 1 of Schedule 2 of the Notification are also shown.

SCHEDULE 2

[DRAFT] The SMP services conditions imposed on each of the persons identified in Column C of Schedule 1 to this Notification under sections 45, 87 and 88 of the Act as a result of the analysis of the market set out in this Notification, ("SMP conditions")

Part 1: Application, definitions and interpretation of these conditions

1. The SMP conditions in Part 2 of this Schedule shall, except as it is otherwise stated therein, apply to the markets set out in columns A and B of Schedule 1 of this Notification.

2. In this Schedule:

   "**Act**" means the Communications Act 2003;

   ~~"**base year**" means for each relevant year, the period of 12 months ending on 31 March immediately preceding that relevant year;~~

   "**Call**" means a voice call which originates on a public electronic communications network (whether fixed or mobile) and is terminated to a UK mobile number within a number range allocated to, or controlled by, the dominant provider, for which the dominant provider is able to set the termination charge;

   "**call termination charge"** means either a fixed-to-mobile call termination charge or a mobile-to-mobile call termination charge.

   ~~"**charge-setting date**" means each of 1 April, 1 July, 1 October and 1 January of each relevant year;~~

   "**controlling percentage**" means, in relation to each relevant year 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 Year, expressed as a percentage (rounded to one decimal place) of that Retail Prices Index as at the beginning of that period; reduced by:

   (i) for the Second Relevant Year [ ] per cent;
   (ii) for the Third Relevant Year [ ] per cent; and
   (iii) for the Fourth Relevant Year [ ] per cent.

~~(a) see Figure 12 of the explanatory memorandum accompanying this Notification for the percentage on which Ofcom is consulting for O2, Vodafone, T-Mobile, Orange (the successor entity to T-Mobile and Orange following their merger)~~

~~(b) see Figure 12 of the explanatory memorandum accompanying this Notification for the percentage on which Ofcom is consulting for H3G.~~

~~**"Charging Period"** means any of the current charging periods published by the dominant provider;~~

"**charge ceiling"** means for each day in a relevant year, the price calculated in accordance with SMP condition M3.2;

"**dominant provider**" means each of the persons listed in Column C of Schedule 1 to this Notification, other than in relation to SMP condition M2 and SMP condition M3, where it shall have the meaning specified therein;

"**fixed-to-mobile call**" means a Call originating on a fixed public electronic communications network and where the dominant provider sets the charge;

"**fixed-to-mobile call termination charge**" means the charge made by the dominant provider to terminate a fixed-to-mobile call;

"**mobile number**" means a telephone number that is: (a) adopted or otherwise used to identify apparatus designed or adapted to be capable of being used while in motion; and, (b) designated under the National Telephone Numbering Plan ("NTNP") for use in connection with Mobile Services (as that term is defined in the NTNP);

"**mobile-to-mobile call**" means a Call originating on a mobile public electronic communications network of another mobile communications provider and where the dominant provider sets the charge;

"**mobile-to-mobile call termination charge**" means the charge made by the dominant provider to terminate a mobile-to-mobile call;

"**network access**" means the provision of interconnection to the public electronic communications network provided by the dominant provider, together with any services, facilities or arrangements which are necessary for the provision of electronic communications services over that interconnection;

"Ofcom" means the Office of Communications;

"**relevant year**" means any of the following:

(i) the period of 12 months beginning on 1 April 2011 and ending on 31 March 2012 (the "First Relevant Year");

(ii) the period of 12 months beginning on 1 April 2012 and ending on 31 March 2013 (the "Second Relevant Year");

(iii) the period of 12 months beginning on 1 April 2013 and ending on 31 March 2014 (the "Third Relevant Year");

(iv) the period of 12 months beginning on 1 April 2014 and ending on 31 March 2015 (the “Fourth Relevant Year”);

“**Retail Prices Index**” means the index of retail prices compiled by an agency or a public body on behalf of Her Majesty’s Government or a governmental department from time to time in respect of all items (which is the Office for National Statistics at the time of publication of this Notification); and

"**third party**" means a person operating a public electronic communications network.

3. For the purpose of interpreting the SMP conditions in Part 2 of this Schedule:

   (a) except insofar as the context otherwise requires, words or expressions shall have the meaning ascribed to them in paragraph 2 above and otherwise any word or expression shall have the same meaning as it has in the Act;

   (b) the Interpretation Act 1978 shall apply as if each of the SMP conditions were an Act of Parliament; and

   (c) headings and titles shall be disregarded.

Part 2: The SMP conditions

Condition M1 – Requirement to provide network access on reasonable request

M1.1 Where a third party reasonably requests in writing network access, the dominant provider shall provide that network access.

M1.2 The dominant provider shall provide network access in accordance with SMP condition M1.1 as soon as reasonably practicable and on fair and reasonable terms and conditions (including charges) and on such terms and conditions (including charges) as Ofcom may from time to time direct.

M1.3 The charges for Calls as covered by SMP condition M3 below shall be as set out in that condition for those defined dominant providers, but only for the duration of that condition.

M1.4 The dominant provider shall comply with any direction Ofcom may make from time to time under this SMP condition.

Condition M2 – Requirement not to unduly discriminate

M2 The dominant provider shall not unduly discriminate against particular persons or against a particular description of persons, in relation to matters connected with network access.

For the purposes of SMP condition M2:

“**dominant provider**” means [H3G], [02], [Vodafone] and [Everything Everywhere].

Condition M3 – Control of termination charges

~~**M3.1** Except as Ofcom may otherwise consent under SMP condition M3.8, the dominant provider shall ensure that, during any relevant year, the average call termination charge as calculated in each of SMP conditions M 3.2(a) and M 3.2(b) separately, and M3.3 does not exceed the maximum average charge.~~

M3.1 The dominant provider shall ensure that for each Call on any day, during any relevant year, the call termination charge does not exceed the charge ceiling.

~~**M3.2** In this SMP condition, the average call termination charge is specified separately as follows:~~

~~(a) With respect to fixed-to-mobile calls, the average of the fixed-to-mobile call termination charges during the relevant year in question, weighted according to:~~

~~(i) the profile by Charging Period of the dominant provider's fixed-to-mobile call minutes; and,~~

~~(ii) the corresponding volumes by quarter of the dominant provider's fixed-to-mobile call minutes,~~

~~in the base year.~~

~~(b) With respect to mobile-to-mobile calls, the average of the mobile-to-mobile call termination charges during the relevant year in question, weighted according to:~~

~~(i) the profile by Charging Period of the dominant provider's mobile-to-mobile call minutes; and,~~

~~(ii) the corresponding volumes by quarter of the dominant provider's mobile-to-mobile call minutes,~~

~~in the base year.~~

~~(c) Where the dominant provider applies the same call termination charge for each of fixed-to-mobile and mobile-to-mobile calls, the calculations in SMP conditions M 3.2(a) and M 3.2(b) may be aggregated.~~

M3.2 The charge ceiling is:

(a) for any Call on a day in the First Relevant Year, [….] pence per minute;

(b) for any Call on a day in the Second Relevant year, Third Relevant Year or Fourth Relevant Year:

a sum equal to the charge ceiling, expressed in pence per minute, in the relevant year preceding the relevant year in which the Call was made, multiplied by the sum of 100% and also multiplied by the controlling percentage for the relevant year in which the Call was made (without rounding up or down) and expressed as being pence per minute, which total is then rounded to three decimal places (and expressed as being pence per minute).

~~**M3.3** For the purposes of calculating the average call termination charge separately for fixed-to-mobile calls and mobile-to-mobile calls where any call termination charges are in force during a part only of the relevant year (commencing or ending at a date in the course of the relevant year), the weighting shall be derived from:~~

> ~~(a) the profile by Charging Period of the dominant provider's separate fixed-to-mobile and mobile-to-mobile call minutes; and~~
>
> ~~(b) the corresponding volumes by quarter of the dominant provider's separate fixed-to-mobile and mobile-to-mobile call minutes,~~

~~in the corresponding part of the base year.~~

~~Where the dominant provider applies the same call termination charge for both fixed-to-mobile and mobile-to-mobile calls during a part only of the relevant year (commencing or ending at a date in the course of the relevant year), the above calculations may be aggregated.~~

~~**M3.4** The dominant provider shall:~~

~~(a) only make changes to its call termination charges on a charge-setting date in each relevant year;~~

~~(b) only set one call termination charge rate for each of weekday daytime, weekday evening and weekend Charging Periods; and~~

~~(c) ensure that except where a change is made on the 1 April each call termination charge (corresponding to a given Charging Period) is not increased by more than 20% on a charge-setting date.~~

~~**M3.5** For the purposes of this SMP condition, the maximum average charge means:~~

> ~~(a) for the purpose of the First Relevant Year,~~
>
> > ~~(i) [….] pence per minute (see Figure 12 of the explanatory memorandum accompanying this Notification for the maximum average charges on which Ofcom is consulting).~~
>
> ~~(b) for the purpose of the Second, Third and Fourth Relevant Years:~~

~~the maximum average charge in the base year multiplied by the sum of 100% and the Controlling Percentage for that relevant year, without rounding up or down.~~

M3.36 The dominant provider shall not make any call termination charge for:

> (a) a Call which terminates on a recorded announcement provided by the dominant provider informing the caller of an inability to complete that Call so as to establish a two-way path where the mobile handset used by the called party is switched off, or rings and remains unanswered, or where coverage is not available from the dominant provider's public electronic communications network; and
>
> (b) an unanswered Call which is diverted in respect of the period before that Call is answered.

~~**M3.7** Notwithstanding SMP Condition M3.1 above:~~

~~(a) if the average call termination charge exceeds the maximum average charge for the First, Second or Third Relevant Year, the dominant provider shall make such adjustments to its termination charges and by such day in the following relevant year as Ofcom may direct for the purpose of remedying that excess. Such adjustments in the Second, Third or Fourth Relevant Year shall not be relevant for the purpose of establishing compliance with SMP condition M3.1 above in that relevant year; and,~~

~~(b) if it appears to Ofcom that the dominant provider is likely to fail to secure that the average call termination charge for the Fourth Relevant Year does not exceed the maximum average charge for that year, the dominant provider shall adjust its call termination charges by such day in that relevant year as Ofcom may direct for the purpose of avoiding that failure.~~

~~**M3.8** Where the average call termination charge is less than the maximum average charge for the First, Second or Third Relevant Year, the dominant provider shall not adjust its termination charges in the following relevant year to recover the difference between the average call termination charge and the maximum average charge for the First, Second or Third Relevant Year, unless Ofcom have given their prior written consent to such adjustments. Such adjustments in the Second, Third or Fourth Relevant Year shall not be relevant for the purpose of establishing compliance with SMP condition M3.1 in that relevant year.~~

M3.4~~9~~ Without prejudice to Ofcom's statutory information gathering powers, the dominant provider shall provide to Ofcom in writing any~~the~~ information reasonably required by Ofcom ~~necessary for the dominant provider~~ to demonstrate compliance with this SMP condition at any time during the Relevant Year upon reasonable notice.~~, this includes:~~

~~(a) no later than three months after the start of each relevant year, the following information:~~

~~I. the total volume of Call minutes to be used in the calculation of the average call termination charge in the relevant year in question broken down in accordance with SMP conditions M3.2 and M3.3;~~

~~II. all data used to build the volume of Call minutes in SMP Condition M 3.9 (a) I. to ensure the correct call types (by type and amount) have been included in and excluded from the calculation of the average call termination charge;~~

~~III. an explanation of how the volume data has been collected and prepared; and~~

~~IV. any other information (including data) that the dominant provider has used to calculate the volume information provided.~~

~~(b) no later than the day on which the dominant provider notifies Ofcom of its final rate change for each relevant year, the following information:~~

~~I. pursuant to SMP condition M3.5, the maximum average charge the dominant provider has applied for the relevant year in question;~~

~~II. the average call termination charge and the calculation of this charge for that relevant year;~~

~~III. the call termination charges made by the dominant provider in that year;~~

~~IV. any changes to the volume data provided under SMP condition M 3.9(a); and~~

~~V. any other information (including data) that the dominant provider has used to calculate the average call termination charge.~~

M3.5~~10~~ The dominant provider shall comply with any direction Ofcom may make from time to time under this SMP condition.

For the purposes of SMP condition M3 only:

"**dominant provider**" means [H3G], [02], [Vodafone] and [Everything Everywhere].

Condition M4 – Requirement to publish charges

M4.1 Unless Ofcom otherwise consents in writing, the dominant provider shall publish its charges for the provision of network access and act in the manner set out below.

M4.2 The dominant provider shall publish its call termination charges, separately from any of its other interconnection charges (including other termination charges).

M4.3 The dominant provider shall, on or before the earlier of: (a) the first charge-setting date in the First Relevant Year; or, (b) the date that this SMP condition comes into force, publish its charges on which it provides network access.

M4.4 The dominant provider shall provide any proposed amendment to the charges on which it provides network access or in relation to any charges for new network access (an "Access Charge Change Notice") to Ofcom five working days before providing them to the organisation that is notified first and it shall publish any amendment or new charge not less than twenty eight (28) days before any such amendment or new charge comes into effect and consistent with SMP condition M3.1.

M4.5 Publication of the information in SMP conditions M4.3 and M4.4 above shall be effected by:

(a) sending a copy of such information or any appropriate parts of it to any person who may reasonably request such a copy; and

(b) placing a readily accessible copy of such information on any relevant website operated or controlled by the dominant provider.

M4.6 The dominant provider shall ensure that an Access Charge Change Notice includes:

(a) a description of the proposed new charge for the network access in question;

(b) where applicable, the current charge for the network access in question; and

(c) the date on which or the period for which any amendments to charges will take effect (the "effective date").

M4.7 The dominant provider shall not apply any new charge identified in an Access Charge Change Notice before the effective date.