OFCOM CONSULTATION ON WHOLESALE MOBILE CALL TERMINATION

28TH JUNE 2010

Cable&Wireless Worldwide

INTRODUCTION

Cable&Wireless Worldwide welcomes the opportunity to comment on Ofcom's Market Review of Mobile Termination Rates which sets out proposals to set termination rates for the next charge control period commencing on the 1st April 2010. We have not set out answers to the specific questions raised by Ofcom rather we set out comments in relation to the key aspects of the consultation document which have most relevance to us. In particular our comments relate to the following areas:

- The adoption of pure LRIC
- Assessment of costs
- The Glide Path
- Ofcom's proposals to end flip flopping
- SMP Designation
- Reciprocity
- Notification obligations

THE ADOPTION OF PURE LRIC (LRMC)

In our response to the first consultation on this market review in 2009, we set out our view that our preferred option for the future regulation of Mobile Termination Rates (MTRs) was the adoption of pure LRIC (or LRMC). Our view is largely influenced by the belief that MTRs are currently well above cost and that they result in a transfer of value from fixed network customers to the mobile operators. In addition, the effect of high mobile termination rates makes it very difficult for fixed operators to include calls to mobile in all inclusive packages, in the way that the mobile operators can, and this encourages consumers to use their mobile rather than fixed phone even if it may not be the most efficient choice. Having read Ofcom's proposals for the adoption of pure LRIC as the basis of the next charge control we remain of the same opinion and support Ofcom's proposals to reduce MTRs to 0.5ppm over a four year glidepath.

Cable&Wireless Worldwide supports Ofcom's proposal to base MTRs on pure LRIC for a number of reasons including:

- Reducing the difference between fixed termination rates and mobile termination rates will help drive efficient competition between fixed and mobile networks and should result in retail prices that help consumers make cost efficient choices when making calls to mobile handsets;
- It will result in a greater proportion of all mobile costs being recovered through charges that are constrained by competition rather than through charges that have to be constrained through regulation;
- The removal of common costs from the regulated charges reduces some of the room for argument over the implementation of charge controls which has been a problem each time a new charge control has been put in place. Although the move to pure LRIC itself is likely to be fiercely contested, once it is in place there should be less to argue about and less financial value associated with a challenge to an assessment of costs;
- The pure LRIC approach aligns Ofcom with the EU Recommendation for mobile termination rates;
- The lower rates that result from the pure LRIC approach remove some of the incentives for arbitrage business models that involve mobile number ranges being used for services that aren't truly mobile.

COSTS

Cable&Wireless Worldwide does not intend to comment on whether Ofcom has made the correct assessment of the MNOs' costs. However it is clear that in setting the charge control on the basis of the costs of an operator with a market share of 25% the efficiencies that such an operator can enjoy will be significantly higher than those that can be achieved by a new market entrant. As such it is highly likely that the cost base of a new market entrant will be higher than that of the 4 MNOs. There is a risk that in setting MTRs on this basis of reciprocity across the market that potential market entrants will find it difficult to justify investment needed in order to actually enter the market. This is particularly the case where the new market entrant does not have either the range of services or the customer base available to it in order to ensure that it can recover its costs .

In setting the level of efficiency at 25% market share Ofcom must ensure that it is not discouraging future investment in the market. While we agree that regulation should not encourage inefficient market entry there is a risk that if the assessment of efficiency is set too high this will make investment difficult and will therefore discourage market entry and innovation.

The EU recommendation sets out that in certain circumstances asymmetry in MTRs may be possible for a period of up to four years where a new service is innovative and where the costs are higher in the initial period of market entry. To date in resolving disputes regarding the MTRs of new market entrants Ofcom has taken a sufficiently long term view of new entrants' costs so as to conclude that they have not been above current regulated MTRs but as the regulated MTRs fall it is more likely that new entrants costs will exceed the regulated rates of the established MNOs. Going forward the challenge on new market entrants will be even greater and Ofcom must be prepared where necessary to allow a period of asymmetry in rates where this is appropriate. Failure to do so will clearly deter investment.

THE GLIDE PATH

Cable&Wireless Worldwide supports Ofcom's proposed use of a glidepath to move regulated rates from their position today to the pure LRIC based target in 2014/15.

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Glidepaths are a tried and tested method for controlling charges in wholesale markets where regulation is required as they ensure the regulated entity retains the incentives to improve efficiency and beat the targets set by regulation. Particularly with changes of the magnitude proposed by Ofcom in this case, it is important that not only the regulated entity by other impacted entites get time to adjust to the changes being made.

As both a major fixed operator and an FMC operator Cable&Wireless Worldwide is itself significantly impacted by the changes and those impacts are a mixture of both positive and negative effects. Specifically in terms of our relatively new FMC proposition the investment case was made on the assumptions of MTRs that were materially higher than those now proposed and therefore that case will be altered. It is important that we have time to react to changes in termination rates and the glidepath approach achieves that.

Ofcom considers whether to depart from its normal glidepath that provides a constant annual percentage reduction in each year and instead require a constant absolute change each year. While either approach provides the benefits that we seek to achieve from the glidepath we see no reason to depart from the normal approach in this case. The two factors that set this charge control out from others that Ofcom has put in place are the switch from LRIC+ to pure LRIC and the extent of the reduction required over the period but neither justifies a change to the normal approach. In particular the EU recommendation requires the adoption of pure LRIC in the first year of the proposed charge control rather than the end and the there is no suggestion from Ofcom’s cost modelling that the shape of the glidepath pushes MTRs below cost and any point during the control.

FLIP FLOPPING

We are pleased that Ofcom has decided to address the practice of “flip flopping” whereby the MNOs make frequent rate changes in order to benefit from months with five weekends compared to the corresponding month of the previous year of the charge control that had four weekends. In our response to Ofcom's first market review consultation in 2009, C&W Worldwide set out its view that not only does the frequency of rate changes make it difficult to measure the MNO's compliance with the charge control but is also places an administrative burden on operators to keep changing prices.

Ofcom has set out four possible approaches to flip flopping and has expressed a preference for option 2 whereby the frequency in rate charges is limited to once a quarter and the extent of the rate change is limited to a 20% increase. We agree that option 2 represents an improvement in the current situation and would be happy to see that option put in place.

SMP DESIGNATION

We do not object in principle to Ofcom's market definition or to necessarily being designated as having SMP as the impact on us is not dissimilar to what we face today. Following the determination of a dispute by Ofcom between C&W Worldwide and T-Mobile over C&W Worldwide's MTRs for its Fixed Mobile Converged service, we have charged the same termination rates as the MNOs. This situation will clearly remain unaltered by the SMP designation. However despite charging the same MTRs as the mobile operators we have had considerable difficulty with some MNOs excluding calls to our number ranges from their bundles of inclusive minutes – this has been bad for the perspective of customer perception of our service and bad for the consumer as it is has been charged more to call our service than when calling other mobile numbers. It is unclear whether placing SMP designations on all mobile number range holders will prevent this practice and Ofcom should be prepared to take action if it does not.

RECIPROCITY

As set out above we don't object in principle to being designated as having SMP however we are concerned that Ofcom's approach to future charge control for MTRs fails to recognise that there are different cost models underlying services than just those of the 4 MNOs. Placing obligations to provide services on fair and reasonable terms is aimed at ensuring reciprocity in rates across the market, however for new market entrant this assumes that the cost model underlying its business must be the same or largely similar to that of the established MNOs. We don't believe this is the case as new market entrants face higher costs at the start of market launch which under the proposed charge control they will struggle to recoup.

It is unclear whether in placing SMP obligations on all operators to provide service on fair and reasonable terms, whether this will also mean that new market entrants will be forced to copy the time of day charges and frequency of rate changes that will apply to the MNOs. We think clarity is required around these issues.

NOTIFICATION

In the consultation document Ofcom sets out its proposal that rate changes will be notified to Ofcom 5 working days prior to notification to the market. Cable&Wireless Worldwide is unclear whether this applies just to the 4 MNOs or whether it will apply to all mobile number range holders who are designated as having SMP. In the latter case it is unclear what the benefit of notification to Ofcom would be given that the MTRs of this group of operators are not directly regulated. Moreover. it is unclear what action Ofcom would take if it is dissatisfied with the rate changes proposed by the operator. We believe clarity is required on this issue.

CONCLUSION

We are supportive of Ofcom's conclusions that it should continue to regulate MTRs and that these rates should be reduced. MTRs are currently too high and result in an imbalance in competition between the fixed and the mobile industries. In particular we support Ofcom's proposals to:

- Change the basis for setting regulated MTRs to one based upon pure LRIC cost rather than the LRIC+ method used in previous charge controls;
- Reduce the level of the charges to Ofcom's current view of pure LRIC cost over a 4 year period through the use of an RPI-X glidepath;
- Put in place measures that will prevent the practice known as "flip flopping"