



Undue discrimination by SMP providers

How Ofcom will investigate potential contraventions on competition grounds of Requirements not to unduly discriminate imposed on SMP providers

Consultation

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Section 1

Summary

Introduction

- 1.1 Ofcom has imposed regulation on some companies it has found to be dominant, requiring them not to unduly discriminate, to prevent them from using their dominance to the detriment of competition and consumers.
- 1.2 This consultation proposes how Ofcom may investigate potential contraventions of these requirements. The current approach was designed before the Communications Act 2003 was made law and we consider that the approach should be reviewed in light of our experience of enforcing the Act¹.
- 1.3 The consultation will be of interest to:
 - SMP Providers² that are subject to a *Requirement not to unduly discriminate*; and
 - the customers and competitors of those providers within the markets affected; and
 - other stakeholders who are interested in the effectiveness of competition within communications markets.
- 1.4 This consultation does not cover Ofcom's approach to investigating potential exploitation of customers on equality or fairness grounds that may be prohibited by the same requirements; or other discrimination prohibitions imposed under the Act; or investigations of compliance with the Competition Act 1998.
- 1.5 Feedback on these proposals is welcomed. Please send your response to katie.miller@ofcom.org.uk by **5pm on 8th September 2005**. Further details on how to engage with this consultation are set out in annex 3.

Summary

- 1.6 This consultation considers *Requirements not to unduly discriminate* between customers, on competition grounds, imposed on providers that Ofcom (the Office of Communications) considers to have significant market power (SMP providers).
- 1.7 A typical *Requirement not to unduly discriminate*, imposed on SMP providers under section 45 of the Communications Act 2003 (the Act) reads:

The Dominant Provider shall not unduly discriminate against particular persons or against a particular description of persons, in relation to [Network Access].

Section 4 sets out the legal basis for Requirements not to unduly discriminate.

- 1.8 The approach to investigating compliance with these requirements, which is proposed in this consultation, has two parts.

¹ Throughout this document *the Act* refers to the Communications Act 2003

² *SMP providers* means providers Ofcom considers to have significant market power

- 1.9 Firstly, in all cases, the proposal sets out the questions that may be considered during an investigation. This would not prevent Ofcom from considering each potential contravention on the facts of the case.
- Ofcom will consider whether any differences in transaction conditions (e.g. the product, its reliability, timing of provision, information about the product) offered to two customers reflect relevant differences in the customers' circumstances; or
 - whether any relevant similarities in customer's circumstances are reflected in transaction conditions offered to two customers.
 - Ofcom will consider whether any differences (or similarities) in transaction conditions that are not objectively justified by relevant differences (or similarities) in the customers' circumstances might harm competition.
- 1.10 In determining whether any differences (or similarities) identified might harm competition Ofcom will consider:
- the capability that the behaviour had to harm competition; and
 - the capability that the behaviour has to harm competition; and
 - the capability that the behaviour will have to harm competition if it is allowed to continue.
- 1.11 Secondly, Ofcom proposes that differences in non-price transaction conditions³ offered by an SMP provider in favour of its own downstream business (a vertically integrated SMP provider) should be treated as a special case.
- 1.12 That is, Ofcom may presume undue discrimination when a vertically integrated SMP provider offers the same price, but different non-price transaction conditions to an external wholesale customer, when compared to a downstream business owned by the SMP provider.
- 1.13 The SMP provider will then have the opportunity to provide evidence demonstrating that differences are objectively justified, and Ofcom will consider any evidence provided in light of the questions above.
- 1.14 The reasons for reviewing our approach and the benefits of guidelines are addressed in section 2. The meaning of undue discrimination and the reasons why non-price differences offered by vertically integrated providers are considered a special case are covered in section 3. The proposals are contained in section 5. A description of some non-price transaction conditions that may lead to undue discrimination are given in annex 1.

³ *non-price transaction* conditions mean features of a product other than price (see glossary)

Section 2

Introduction

- 2.1 This section explains both the benefit of guidelines and why Ofcom considers it is appropriate to review the current approach to undue discrimination.

The role of guidance

- 2.2 Guidelines contribute to effective regulation by providing transparency and generating understanding.
- Guidelines encourage compliance by explaining conditions imposed, thereby ensuring that SMP providers understand their obligations and enabling potential customers to identify contraventions.
 - Guidelines promote effective competition by reducing any difficulty SMP providers have distinguishing between conduct that might result in penalties and conduct that would not. If SMP providers are unable to make such distinctions, there is a risk that they will be deterred from normal competitive behaviour.
 - They also help to frame an effective complaint, or an effective defence, in the event that an SMP provider is suspected of contravening a condition.
- 2.3 One of Ofcom's regulatory principles is that Ofcom will regulate in a transparent manner⁴. Guidelines are an important means to achieving this principle and to increasing understanding of Ofcom's policy objectives and approach to regulation.

Benefit of reviewing Ofcom's approach to undue discrimination

- 2.4 There are three reasons that have prompted Ofcom to review its approach to undue discrimination. Firstly, the current approach was determined in advance of the Act becoming law and Ofcom considers that it should review the approach in light of its experiences enforcing the Act. The current approach is set out in Oftel's *Access Guidelines*⁵. The relevant sections of the *Access Guidelines* are set out in annex 2.
- 2.5 Secondly, in the *Strategic review of telecommunications phase 2 consultation*⁶ Ofcom suggested there was a need for a review of the existing approach to investigating undue discrimination. Ofcom set out perceived behavioural problems that might harm competition, particularly within fixed telecoms networks. The consultation responses tended to agree with the description of the problems given.
- 2.6 The effect of the current approach has been to consider harm to competition solely at the time of the evaluation. In effect, this rules out finding a contravention if behaviour ceases during an investigation or if we consider that harm would become material if the behaviour were continued.
- 2.7 Ofcom considers that this approach to materiality is unduly restrictive and inconsistent with our primary duties to promote competition as set out in the Act:

⁴ <http://www.ofcom.org.uk/about/sdrp/>

⁵ *Imposing access obligations under the new EU Directives*, September 2002

⁶ Published 18 November 2004. See http://www.ofcom.org.uk/static/telecoms_review/index.htm

3(1)(b) It shall be the principle duty of Ofcom ...to further the interests of consumers in relevant markets, where appropriate by promoting competition.

4(3) The first Community requirement is a requirement to promote competition [in communications markets].

- 2.8 Third and lastly, we have identified that *Requirements not to unduly discriminate* are not widely understood by SMP providers or their customers. Therefore, we consider that Ofcom should offer further guidance.

Section 3

The meaning of undue discrimination

- 3.1 In this section, we address the definition of undue discrimination in a competition context and explain how it relates to differences in transaction conditions and circumstances of customers.
- 3.2 We also consider particular concerns about non-price differences in transaction conditions offered by vertically integrated SMP providers.

Meaning of undue discrimination for the purpose of the proposed guidelines

- 3.3 This consultation is concerned solely with undue discrimination that is
- on competition grounds,
 - between customers,
 - by SMP providers,
 - which are subject to a Requirement not to unduly discriminate.
- 3.4 Ofcom has wider responsibilities with regard to other forms of discrimination, which are not addressed by this consultation. For example, the Act prohibits discrimination on religious grounds in the sale of advertising opportunities by broadcasters, which is not covered. In particular, the proposed guidelines do not cover exploitation on fairness or equality grounds, although exploitation may be prohibited by the same *requirement not to unduly discriminate*⁷.
- 3.5 Undue discrimination describes when an SMP provider *does not reflect relevant differences* between (or does not reflect relevant similarities in) the circumstances of customers in the transaction conditions it offers, and where such behaviour could harm competition.
- 3.6 For example, an SMP provider would be unduly discriminating if it offered different levels of reliability (a transaction condition) to two customers in similar circumstances for the same product⁸ at the same price (otherwise similar transaction conditions) and this was capable of harming competition between the two customers.
- 3.7 Differences in customers' circumstances may be relevant if they influence the costs of supplying to those customers. For example, a customer's financial status may affect the cost associated with different payment terms. The timing and duration of a contract may be relevant if the degree of risk incorporated varies, or the costs of supply vary over time. Therefore, differences between customers' circumstances may be an objective justification for offering differing transaction conditions.
- 3.8 Ofcom does not consider that the fact that one customer is part of the same company as the SMP provider, will generally constitute an objective justification for a difference in transactions conditions offered.

⁷ Throughout the remainder of this document, references to undue discrimination will mean undue discrimination on competition grounds.

⁸ Throughout this document product is taken to mean goods and / or services.

- 3.9 Competition is likely to be harmed by differences in transaction conditions that do not reflect differences in customers' circumstances, unless those differences lead to an expansion of demand or open up new market segments. Harm may be caused by limiting one customer's ability to compete in a downstream market or by excluding a competitor from a substantial part of a market. Thus, a substantial increase in demand or a new market segment may be an objective justification for offering differing transaction conditions.
- 3.10 Ofcom considers that objective justification for offering two customers different (or similar) transaction conditions can only be assessed on a case-by-case basis; by considering the circumstances of the customers and the capability of harming competition.

Non-price differences in transaction conditions offered by a vertically integrated SMP provider

- 3.11 In the case of non-price differences in transaction conditions, offered by a vertically integrated SMP provider in wholesale markets, Ofcom may not apply a case-by-case approach. This is due to the particular features of this type of behaviour and the features of communications markets.
- 3.12 In communications markets the incentives to unduly discriminate to gain commercial advantage are significant:
- There are increasing returns and economies of scope achieved from a large customer base, meaning that firms need to achieve scale in order to maximise their chances of becoming profitable overall or in particular products.
 - There are significant network effects; new customers are attracted to a provider that already has a large customer base. So a provider is motivated to drive product take-up and to achieve first-mover advantage for new products (particularly where products do not work with competitors' products).
 - Technology changes quickly and can deliver a decisive advantage, requiring significant risks to be taken on investments.
- 3.13 The incentives are greater still for a vertically integrated SMP provider to engage in some forms of undue discrimination, which is reflected in the focus of the Directives (see section 4). Vertically integrated SMP providers have a particular incentive to favour an internal customer over an external customer where the customers compete in a downstream market. A vertically integrated provider with upstream SMP will be motivated to lever this market power downstream to maximise profits.
- 3.14 These SMP providers also have incentives to unduly discriminate using differences in non-price transaction conditions instead of differences in prices. Excessive prices offered to external customers can be largely controlled by setting price controls; and predatory pricing (pricing below cost) comes at a cost. In contrast, non-price differences in transaction conditions are often not costly to the SMP provider.
- 3.15 Non-price differences in transaction conditions could be differences in:
- the functionality of the product supplied,
 - timing of provision,
 - the reliability and efficiency of transactional processes; or

- availability of information that supports the purchase or supports the use of the product.

Differences in non-price transaction conditions rarely benefit competition. They are unlikely to open new market segments or to increase demand substantially.

Examples of non-price differences that may be capable of harming competition are described in annex 1.

- 3.16 The incentives for a vertically integrated SMP provider to offer differences in non-price transaction conditions are further increased by the relative difficulty of identifying differences. An external customer may find it difficult to identify the transaction conditions that an SMP provider offers to an internal customer - its own downstream business.
- 3.17 These incentives – deriving from the nature of communications markets, the relationship between a vertically integrated SMP provider and an internal customer, and from the advantages of using non-price differences over price differences - do not mean there is always intent. The incentives described above equally apply to avoiding unintended undue discrimination.
- 3.18 Ofcom considers that non-price differences in transaction conditions offered by a vertically integrated SMP provider favouring an internal customer can be presumed to harm competition given the incentives for such behaviour and the lack of benefits that may accrue.

Section 4

Requirements imposed on SMP providers not to unduly discriminate

4.1 *Requirements not to unduly discriminate* derive from European Directives, which, in the UK, are transposed into the Act. This section describes this legal basis for the requirements imposed on SMP providers.

4.2 It sets out:

- principles and non-discrimination obligations in the Directives;
- transposition of the Directives into the Act in wholesale markets, leased line⁹ markets and retail markets;
- Requirements not to unduly discriminate; and
- providers and markets where requirements are currently imposed.

The current regulatory framework

4.3 SMP providers are regulated by Ofcom under the Act, which implements the EC Directives¹⁰. The basis and derivation of Requirements not to unduly discriminate differ between wholesale markets, leased line markets and other retail markets.

4.4 SMP has been defined so that it is equivalent to the competition law concept of dominance. The Framework Directive¹¹ states that:

An undertaking shall be deemed to have significant market power if, either individually or jointly with others, it enjoys a position equivalent to dominance, that is to say a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers.

4.5 Ofcom is required to impose conditions on all SMP providers, where appropriate, where those conditions are objectively justifiable, not unduly discriminatory, proportionate and transparent¹². In most cases where a provider has been found to have SMP, Ofcom (or Oftel) has imposed a requirement prohibiting undue discrimination. A summary of these is set out at paragraph 4.23 below.

Wholesale markets

4.6 Ex ante remedies available to Ofcom in respect of wholesale markets are set out in the Access Directive¹³. One of these is an obligation of non-discrimination as set out below:

⁹ Leased lines are dedicated telephone lines, often used by businesses for data transfer

¹⁰ The Framework Directive (2002/21/EC), the Authorisation Directive (2002/20/EC), the Access Directive (2002/19/EC) and the Universal Service Directive (2002/22/EC).

¹¹ Article 14 of the Framework Directive

¹² Section 47 of the Act

¹³ Article 10 (2)

- 4.7 Obligations of non-discrimination shall ensure, in particular, that the operator applies equivalent conditions in equivalent circumstances to other undertakings providing equivalent services, and provides services and information to others under the same conditions and of the same quality as it provides for its own services, or those of its subsidiaries or partners.

This obligation is focused on vertically integrated providers since it highlights the need to offer customers equivalent conditions to those it “provides for its own services, or those of its subsidiaries or partners”. This observation does not limit the application of non-discrimination under the Directives since it exemplifies one form “in particular”.

- 4.8 The preamble to the Access Directive¹⁴ describes the need to prohibit undue discrimination that harms competition in the following terms:

The principle of non-discrimination ensures that undertakings with market power do not distort competition, in particular where they are vertically integrated undertakings that supply services to undertakings with whom they compete in downstream markets.

- 4.9 The provisions of the Access Directive allowing for non-discrimination obligations are implemented in the UK by section 87 of the Act¹⁵, which states:

The SMP conditions authorised by this section also include one or more of the following –

(a) a condition requiring the dominant provider not to discriminate unduly against particular persons, or against a particular description of persons, in relation to matters connected with network access to the relevant network or with the availability of the relevant facilities;

- 4.10 The term 'non-discrimination' is transposed into the Act by the term 'undue discrimination' reflecting previous telecoms regulation in the UK.

Leased lines

- 4.11 SMP conditions imposed on leased lines providers derive instead from the Universal Service Directive¹⁶:

[Ofcom is] to ensure that the organisations identified as having significant market power pursuant Article 18(1) adhere to the principle of non-discrimination when providing leased lines referred to in Article 18. Those organisations are to apply similar conditions in similar circumstances to organisations providing similar services, and are to provide leased lines to others under the same conditions and of the same quality as they provide for their own services, or those of their subsidiaries or partners, where applicable.

- 4.12 Section 92(3) of the Act implements this part of the Universal Service Directive and is set out below:

The SMP conditions authorised by this section are conditions for applying, so far as required by the provisions for the time being contained in Annex VII to the

¹⁴ Recital 17, Access Directive (2002/19/EC)

¹⁵ Article 10 in particular has been implemented in the UK by section 87(6)(a) of the Act

¹⁶ Annex VII

Universal Service Directive, the principles of non-discrimination, cost orientation and transparency in relation to the leased lines identified as mentioned in subsection (1).

Retail markets

- 4.13 Requirements imposed on SMP providers in retail markets also derive from the Universal Service Directive. Recital 26 of the Directive sets out the principles that apply in retail markets:

In general for reasons of efficiency and to encourage effective competition, it is important that the services provided by an undertaking with significant market power reflect costs. For reasons of efficiency and social reasons, end-user tariffs should reflect demand conditions as well as cost conditions, provided that this does not result in distortions of competition. There is a risk that an undertaking with significant market power may act in various ways to inhibit entry or distort competition, for example by charging excessive prices, setting predatory prices, compulsory bundling of retail services or showing undue preference to certain customers. Therefore, [Ofcom] should have powers to impose, as a last resort and after due consideration, retail regulation on an undertaking with significant market power.

- 4.14 Requirements in retail markets have more than just a competition purpose; efficiency and social reasons are other purposes highlighted by the recital. Therefore, *Requirements not to unduly discriminate* may also be imposed to discourage exploitation of customers on fairness or equality grounds.
- 4.15 Article 17(2) of the Directive sets out the regulatory controls available to Ofcom for retail products where the provider has been notified as having SMP:

The obligations imposed may include requirements that the identified undertakings do not charge excessive prices, inhibit market entry or restrict competition by setting predatory prices, show undue preference to specific end-users or unreasonably bundle services.

- 4.16 This is implemented by section 91(5) of the Act:

The SMP conditions authorised by this section are conditions imposing on the dominant provider such regulatory controls as OFCOM may from time to time direct in relation to the provision by that provider of any public electronic communications service to the end-users of that service.

- 4.17 Ofcom has imposed *Requirements not to unduly discriminate* in a number of retail markets which are listed in paragraph 4.23.

Requirements not to unduly discriminate

- 4.18 The SMP conditions prohibiting undue discrimination generally follow a standard format, whether in wholesale, retail or leased lines markets.
- 4.19 For example, the requirement on BT not to unduly discriminate in the supply of partial private circuits (PPCs)¹⁷ is set out below:

¹⁷ Condition G2 - *Requirement not to unduly discriminate* in traditional interface symmetric broadband origination markets (capacity up to 8Mb/s).

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.

In this Condition, the Dominant Provider may be deemed to have shown undue discrimination if it unfairly favours to a material extent an activity carried on by it so as to place at a competitive disadvantage persons competing with the Dominant Provider.

4.20 The second paragraph of this requirement is an example and does not illustrate the extent of the obligation described in the first paragraph.

4.21 An example¹⁸ requirement imposed on Kingston from a retail market (fixed narrowband, or ordinary telephone lines) goes as follows:

The Dominant Provider shall not unduly discriminate against particular persons or a particular description of persons in relation to services offered.

Nothing done in any manner by the Dominant Provider shall be regarded as undue discrimination under this condition if and to the extent that the Dominant Provider is required or expressly permitted to do such thing in that manner by or under any condition set under section 45 of the Act which applies to the Dominant Provider.

4.22 The second paragraph of this form reflects that this requirement coexists with an obligation to provide a universal service, available to everyone across the Hull area.

SMP providers and markets currently subject to *Requirements not to unduly discriminate*

4.23 Those SMP providers that are currently subject to such a requirement are listed below.

¹⁸ Condition DA1 – *Requirement not to unduly discriminate*

Markets¹⁹**SMP providers**

wholesale residential and business analogue exchange line services	BT, Kingston
wholesale residential and business ISDN2 exchange line services	BT, Kingston
wholesale ISDN30 exchange line services	BT, Kingston
call origination on fixed public narrowband networks	BT, Kingston
fixed geographic call termination	BT, Kingston
traditional interface symmetric broadband origination	BT, Kingston
alternative interface symmetric broadband origination	BT, Kingston
traditional interface retail leased lines up to 8Mb/s	BT, Kingston
wholesale local access services	BT, Kingston
asymmetric broadband origination	BT, Kingston
broadband conveyance	BT, Kingston
wholesale trunk segments	BT
local-tandem and inter-tandem conveyance and transit on fixed public narrowband networks	BT
single transit on fixed public narrowband networks	BT
wholesale international call conveyance (specific routes)	BT, C&W
wholesale unmetered narrowband internet termination	Kingston
wholesale mobile call termination	O2, Orange, T-Mobile, Vodafone
access to terrestrial transmission masts and sites	Arqiva (formally ntl:broadcast), Crown Castle

¹⁹ For full definitions of the markets listed here, please refer to the market reviews available at www.ofcom.org.uk

Section 5

Ofcom's proposals

- 5.1 This section sets out Ofcom's proposals for investigating potential contraventions, of a *requirement not to unduly discriminate* imposed on an SMP provider under section 45 of the Act.
- 5.2 The proposals apply to investigations resulting from a complaint made to Ofcom; as part of a dispute that it has been requested to resolve; or investigations made on Ofcom's own initiative. The proposed approach will not apply to the exercise of Ofcom's powers or functions under the Competition Act 1998.
- 5.3 Our proposals are in two parts. Firstly, we outline the questions that may be considered in all cases. Secondly, we set out a presumption that Ofcom may make in special cases, which may be rebutted by the SMP provider.
- 5.4 Although the guidelines, when finalised, will set out the approach Ofcom expects to take, they do not have binding legal effect. Ofcom will consider each case on its own merits. We will only apply the proposed approach where it is appropriate to do so and in the event that Ofcom decides to depart from the guidelines, we will set out our reasons.
- 5.5 Guidelines are not a substitute for the Act or conditions made under it. They should be read in conjunction with these legal instruments and relevant Community and UK case law. Anyone in doubt about how they might be affected should seek their own legal advice.
- 5.6 Ofcom expects to review its approach from time to time as its experience of regulation in the relevant markets grows and as competition in the relevant markets develops. The proposals contained in this consultation would replace the approach described in sections 3.4 to 3.14 and A3.6 to A3.7 of Oftel's Access Guidelines (set out in annex 2).

Questions Ofcom will consider before finding a contravention

- 5.7 The first part of Ofcom's proposals sets out the questions that may be considered. This will enable parties to an investigation to engage effectively and efficiently with our investigation process.
- 5.8 Before finding a contravention has occurred or is occurring Ofcom will consider two questions to determine whether there is any objective justification for the behaviour under investigation. These questions will be considered in cases based on price or based on non-price differences in transaction conditions.
- 5.9 Firstly, Ofcom will consider whether any differences in transaction conditions offered to two customers reflect relevant differences in the customers' circumstances; or whether any relevant similarities in customer's circumstances are reflected in transaction conditions offered to the two customers.
- 5.10 Customers' circumstances will be relevant if they affect the costs of supplying to them.
- 5.11 Secondly, Ofcom will consider whether any differences (or similarities) in transaction conditions not objectively justified by relevant differences (or similarities) in the customers' circumstances might harm competition.

- 5.12 In determining whether any differences (or similarities) identified might harm competition Ofcom will consider:
- the capability that the behaviour had to harm competition; and
 - the capability that the behaviour has to harm competition; and
 - the capability that the behaviour will have to harm competition if it is allowed to continue.

5.13 Therefore, Ofcom will consider the impact of behaviour that has occurred, but has since ceased and of behaviour that has the capability to cause harm to competition in the future, reflecting our responsibilities to promote competition (as described in paragraph 2.7).

5.14 Differences in transaction conditions required or expressly permitted by the Act or by Ofcom, or the result of a choice made by the disadvantaged customer, would not be considered a contravention.

Special cases

5.15 The second part of Ofcom's proposals considers that differences in non-price transaction conditions favouring the internal customer of a vertically integrated provider should be considered a special case.

5.16 In the case of non-price differences in transaction conditions (and similar prices) offered by a vertically integrated SMP provider between an internal and external wholesale customer Ofcom may presume undue discrimination. However, Ofcom will provide the SMP provider with the opportunity to tender evidence to rebut that presumption.

5.17 To rebut this presumption, the SMP provider may demonstrate some objective justification for the differences. This may be relevant differences in the circumstances of the customers, or demonstration that there is no capability of harm to competition, was no capability of harm to competition and will be no capability of harm to competition.

Process

5.18 Finally, there are a number of points to note about the process.

- Usually the first step will be to verify the facts presented to us.
- It may not be necessary to take the proposed questions in order. For example, it may be possible to show there is no impact on competition if the two customers are not competing in any market, before we consider the circumstances of customers.
- If either the conditions or the circumstances of the two customers are identical then determining whether differences (or similarities) in conditions reflect differences (or similarities) in circumstances may not require a detailed analysis.

Question 1: *Do you agree with the proposed approach to investigating potential contraventions of Requirements not to unduly discriminate?*

Annex 1

Examples of non-price transaction conditions

Purpose of section

- A1.1 This section outlines examples of non-price transaction conditions that may be the basis of undue discrimination. We believe that increasing understanding of undue discrimination may encourage compliance.
- A1.2 We consider below a selection of transaction conditions including information, product functionality, performance and availability, and access to marketing opportunities and brands. It is not intended to be comprehensive.
- A1.3 In many cases, the costs of supplying these non-price transaction conditions may not vary significantly between customers. Therefore, there may be no relevant differences in customers' circumstances that would objectively justify offering each customer different transaction conditions.

Information availability

- A1.4 Information transaction conditions cover the availability, timing of availability or accuracy of information. Relevant information will include information that customers would reasonably require in the course of their business such as:
- product information including knowledge of new product development, changes to existing products, pricing packages or investment plans;
 - information about a process surrounding a product upon which the customers are dependent to order, supply or manage a product; or to develop a downstream product efficiently and effectively;
 - information about the technical features of a product such as technical standards; or
 - information about product performance and reliability.
- A1.5 Often, sharing information with a second customer could be a low cost activity and there may be few cases where there is objective justification for giving two customers different levels of access to information. This means that an internal customer of a vertically integrated SMP provider may only have access to these types of information to the extent that similar information is available to external customers.

Product functionality, performance or availability

- A1.6 Product transaction conditions include product features, functionality and reliability, processes for ordering, provisioning and fault repair of the product, as well as the systems they depend upon.
- A1.7 Particular differences that may be unduly discriminatory include:
- differences in lead times or the time taken to repair faults;
 - differences in the number and frequency of faults;

- earlier provision of a product to one customer before other customers; or
- a vertically integrated SMP provider selling a retail product (that is built on a wholesale product) before the wholesale product is available externally.

A1.8 Once a product attribute, such as a level of service, has been made available to one customer, there is unlikely to be any objective justification for denying the same attribute to other customers.

A1.9 An undue discrimination requirement means customers should be granted similar access to products, including the opportunity to trial products and work towards the launch of products on similar timescales.

Marketing opportunities

A1.10 Marketing opportunities include use of a brand, promotional activities and advertising space.

A1.11 These non-price transactional conditions may have the effect of implying that one customer has a unique association with, or preferential access to an upstream product. There may be no objective justification for restricting access to these opportunities between customers. Promotional and marketing activities that seek to lever market power into related markets may result in undue discrimination.

Annex 2

Extracts from Oftel's Access Guidelines

Imposing access obligations under the new EU Directives

A2.1 The following text is taken from Oftel's Access Guidelines. It illustrates the current approach to undue discrimination and simultaneously the elements of the guidelines that Ofcom proposes to withdraw:

Chapter 3

Other obligations that may be imposed on SMP operators under the AID and conditions for the supply of mandated access

Non-discrimination obligations

3.4 Particular competition concerns arise where an undertaking with SMP is vertically integrated. A vertically integrated undertaking may have an incentive to provide products on terms which discriminate in favour of its own business. For this reason, an obligation on a vertically integrated operator with SMP to provide access will nearly always be accompanied by a requirement to do so on non-discriminatory terms.

What is non-discrimination?

3.5 Article 10(2) of the AID states that:

“Obligations of non-discrimination shall ensure, in particular, that the operator applies equivalent conditions in equivalent circumstances to other undertakings providing equivalent services and provides services and information to others under the same conditions and of the same quality as it provides for its own services, or those of its subsidiaries or partners.”

3.6 The main aim of a ‘non-discrimination’ condition (referred to as ‘undue discrimination’ in UK law) is to ensure that a vertically integrated SMP operator does not treat itself in a way that benefits itself, its subsidiaries or its partners in such a way as to have a material adverse effect on competition.

3.7 In practical terms this means that a vertically integrated SMP operator should supply products in such a way that competing service providers are placed in an equivalent position to the retail arm of the SMP operator regarding the information they receive about products and the terms and conditions under which they are made available.

3.8 ‘Non-discrimination’ does not necessarily mean that there should be no differences in treatment between undertakings, rather that any differences should be objectively justifiable, for example by:

- a) differences in underlying costs, or
- b) no material adverse effect of competition.

3.9 Oftel considers that in markets where there is significant market power, there is a rebuttable presumption that a vertically integrated SMP operator

discriminating in favour of its own downstream business would have a material adverse effect on competition.

3.10 In order to ensure compliance with its obligations as regards non-discrimination under the AID, in general, an SMP operator should ensure that:

- a) it applies equivalent conditions in equivalent circumstances to other undertakings providing equivalent services and provides services and information to others under the same conditions and of the same quality as it provides for its own services, or those of its subsidiaries or partners; and
- b) it can objectively justify any differentiation.

3.11 Oftel is likely to consider differences in underlying costs to be a valid justification for making products available on different terms to different parties – ie it may not judge differences in such circumstances to be discriminatory. Oftel would also consider other justifications for differentiation between customers (eg on the grounds of varying degrees of risk presented or overall economic benefit gained from discrimination) on a case by case basis, taking account of any material adverse effect on competition of the action proposed. Annex 3 provides some examples of issues that may arise and how Oftel would be likely to approach these issues.

Non discrimination and new retail product launches

3.12 A vertically integrated operator will, in particular, need to consider its obligations to provide access on non-discriminatory terms when it intends to launch a new retail service and has been designated as having SMP in an associated wholesale market. Such an operator must ensure that, when launching a retail service, it is in a position to meet all reasonable requests for corresponding wholesale products. If this is not the case, the enforcement of the non-discrimination obligation may mean that the SMP operator, in order to comply with its obligation, may have to withdraw the related retail product.

3.13 Oftel would normally consider that provision of an equivalent wholesale product in the wholesale market in which an operator has been designated as having SMP should occur in sufficient time for simultaneous launch by competitors of a competing retail product so as to avoid a material adverse effect on competition.

3.14 Oftel acknowledges that an issue may arise where competing undertakings need to undertake significant network build or technological development to make use of a given wholesale product or where it may take a significant amount of time for the wholesale product to be developed. Oftel will first consider whether it is possible for an interim or alternative product to be supplied that permits operators to compete to the greatest extent possible while technological upgrades are carried out.

Annex 3 Non-Discrimination

Pricing differences

A3.6 A non-discrimination requirement implies that equivalent products should be available at the same price to the SMP operators' retail arm as to competitors.

However, the products provided to other undertakings will not necessarily be identical to those used by the SMP undertaking's retail arm. In particular, the various functions associated with provision of the wholesale product (eg customer support, billing etc) may (depending on the nature of the product concerned) only be relevant to the product as supplied to other undertakings. There may therefore be some justifiable differentiation in pricing based on differences in underlying costs. Differentiation of this kind should in fact be a spur to competition, preserving incentives for operators to invest in their own facilities to enable the service to be provided, rather than relying on others to do so.

Volume discounts

A3.7 These are a common feature of commercial arrangements, and can be advantageous for both parties, allowing the supplier to provide incentives for increased take-up of its product and allowing the purchaser to take advantage of cost-savings arising from economies of scale. Oftel would normally consider volume discounts to be acceptable provided they are applied in a consistent manner treating undertakings in equivalent positions in an equivalent way.

However, where a volume discount has the effect of advantaging the SMP operator, Oftel is likely to consider it unduly discriminatory or anti-competitive. For this reason, Oftel is likely to prohibit the use of volume discounts in markets in which an SMP operator would itself benefit disproportionately by virtue of its relative size over its competitors.

Annex 3

Responding to this consultation

How to respond

Ofcom invites written views and comments on the issues raised in this document, to be made by **5pm on 8th September 2005**.

Ofcom strongly prefers to receive responses as e-mail attachments, in Microsoft Word format, 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 5), among other things to indicate whether or not there are confidentiality issues. The cover sheet can be downloaded from the 'Consultations' section of our website.

Please can you send your response to katie.miller@ofcom.org.uk.

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

Katie Miller
Floor 4
Competition and Markets
Riverside House
2A Southwark Bridge Road
London SE1 9HA

Fax: 020 7981 3333

Note that we do not need a hard copy in addition to an electronic version. Also note that Ofcom will not routinely acknowledge receipt of responses.

It would be helpful if your response could include a direct answer to the question posed in section 5 "Do you agree with the proposed approach to investigating potential contraventions of *Requirements not to unduly discriminate?*". It would also help if you can explain why you hold your views, and how Ofcom's proposals would impact on you.

Further information

If you want to discuss the issues and questions raised in this consultation, or need advice on the appropriate form of response, please contact Katie Miller on 020 7783 4517.

Confidentiality

Ofcom thinks 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 (when respondents confirm on their response cover sheet that this is acceptable).

All comments will be treated as non-confidential unless respondents specify that part or all of the response is confidential and should not be disclosed. Please place any confidential parts of a response in a separate annex, so that non-confidential parts may be published along with the respondent's identity.

Ofcom reserves its power to disclose certain confidential information where this is necessary to fulfil its functions, although in practice it would do so only in limited circumstances.

Please also note that copyright and all other intellectual property in responses will be assumed to be assigned to Ofcom unless specifically retained.

Next steps

Following the end of the consultation period, Ofcom intends to publish a statement in the autumn.

Please note that you can register to get automatic notifications of when Ofcom documents are published, at http://www.ofcom.org.uk/static/subscribe/select_list.htm.

Ofcom's consultation processes

Ofcom is keen to make responding to consultations easy, and has published some consultation principles (see annex 4) which it seeks to follow, including on the length of consultations.

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, whose views are less likely to be obtained in a formal consultation.

If you would like to discuss these issues, or Ofcom's consultation processes more generally, you can alternatively contact Tony Stoller, Director, External Relations, who is Ofcom's consultation champion:

Tony Stoller
Ofcom
Riverside House
2A Southwark Bridge Road
London SE1 9HA
Tel: 020 7981 3550
Fax: 020 7981 3630
E-mail: tony.stoller@ofcom.org.uk

Annex 4

Ofcom's consultation principles

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

Before the consultation

- A4.1 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

- A4.2 We will be clear about who we are consulting, why, on what questions and for how long.
- A4.3 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 version for smaller organisations or individuals who would otherwise not be able to spare the time to share their views.
- A4.4 We will normally allow ten weeks for responses to consultations on issues of general interest.
- A4.5 There will be a person within Ofcom who 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. This individual (who we call the consultation champion) will also be the main person to contact with views on the way we run our consultations.
- A4.6 If we are not able to follow one of these principles, we will explain why. This may be because a particular issue is urgent. If we need to reduce the amount of time we have set aside for a consultation, we will let those concerned know beforehand that this is a 'red flag consultation' which needs their urgent attention.

After the consultation

- A4.7 We will look at each response carefully and with an open mind. We will give reasons for our decisions and will give an account of how the views of those concerned helped shape those decisions.

Annex 5

Consultation response cover sheet

- A5.1 In the interests of transparency, we will publish all consultation responses in full on our website, www.ofcom.org.uk, unless a respondent specifies that all or part of their response is confidential. We will also refer to the contents of a response when explaining our decision, without disclosing the specific information that you wish to remain confidential.
- A5.2 We have produced a cover sheet for responses (see below) and would be very grateful if you could send one with your response. This will speed up our processing of responses, and help to maintain confidentiality by allowing you to state very clearly what you don't want to be published. We will keep your completed cover sheets confidential.
- A5.3 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 cover sheet in a way that allows Ofcom to publish their responses upon receipt, rather than waiting until the consultation period has ended.
- A5.4 We strongly prefer to receive responses in the form of a Microsoft Word attachment to an email. Our website therefore includes an electronic copy of this cover sheet, which you can download from the 'Consultations' section of our website.
- A5.5 Please put any confidential parts of your response in a separate annex to your response, so that they are clearly identified. 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: Undue discrimination by SMP providers

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

CONFIDENTIALITY

What do you want Ofcom to keep confidential?

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 to be confidential, 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. It can be published in full on Ofcom's website, unless otherwise specified on this cover sheet, and I authorise Ofcom to make use of the information in this response to meet its legal requirements. 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 6

Glossary

the Act	the Communications Act 2003
customer's circumstances	the position of a customer that it is relevant to the purchase of a product
Directives	Directives of the European Parliament and of the Council covering electronic communications networks and services and consisting of the Framework Directive (2002/21/EC), the Authorisation Directive (2002/20/EC), the Access Directive (2002/19/EC) and the Universal Service Directive (2002/22/EC)
non-price transaction conditions	features of a product such as the functionality and reliability of the product, the timing of provision, the transactional processes and information that supports the purchase and use of the product etc.
Ofcom	The Office of Communications
predatory pricing	deliberately pricing a product below cost, in order to eliminate a competitor so as to be able to charge excessive prices in the future
products	product is taken to mean goods and/or services throughout this document
SMP	significant market power - equivalent to dominance - economic strength to act independently of customers, competitors and ultimately consumers
SMP providers	communications providers that Ofcom has notified as having significant market power, following a market review
transaction conditions	features of a product including price
vertically integrated SMP providers	an SMP provider that owns a downstream business, such that the SMP providers' customers are also its competitors