Strategic Review of Telecommunications

Summary of responses to Phase 2 consultation

Consultation

Publication date: **31 March 2005**

Contents

Executive summary

Overview

1.1 In November 2004, Ofcom published a consultation document as part of Phase 2 of the Strategic Review of Telecommunications. The consultation document set out Ofcom's proposals for a future regulatory strategy. We have now received around 100 responses to this consultation from a wide range of industry stakeholders comprising operators, consumer groups and industry associations, regional interest groups and other interested parties.

1.2 Because of the number of responses and range of issues addressed, we have produced this summary to enable anyone interested in the Telecoms Review to access more easily the arguments put forward by others in the debate.

With some exceptions, there is broad agreement amongst the industry on the seven regulatory principles set out by Ofcom

1.3 The majority of telecoms operators voiced broad agreement with the seven regulatory principles set out by Ofcom. BT presented a number of modifications to these principles suggesting greater focus on deregulation, forbearance for emerging markets, consistency and transparency in regulation and a "bias towards investment". Other operators, whilst broadly agreeing with the regulatory principles, argued for the need for a clear implementation roadmap for the key principle of ensuring equality of access. Most alternative network operators (altnets) and service providers also argue that a settlement needs to be backed up by strong enforcement and clear sanctions. Some local infrastructure operators, including NTL, Telewest and UK Broadband, however, argue that local access is not an enduring economic bottleneck, and that treating it in this way will harm incentives for alternative infrastructure investment.

Many consumer groups argue that the Telecoms Review is too industry-focused and insufficiently consumer-focused

1.4 A number of consumer groups, including Ofcom's own Consumer Panel, argued that the review was too focused on the internal workings of the telecoms industry, and insufficiently focused on the issues of direct relevance to businesses and consumers. For example, they suggest that Ofcom hasn't clearly explained why its preferred regulatory option would be best for consumers. Because of this, some consumer groups felt that Ofcom had missed an opportunity to address some of the issues, like provision of universal services that are of direct importance to many consumers. This view was supported by the response from the Communications Workers Union (CWU) and Connect, which argues that the key issue for consumers is not simply the availability of competition, but the empowerment of consumers to exercise informed choice in the marketplace.

Most respondents express a preference for Option 3 (Equality of Access)

1.5 A large majority of the respondents (90%), including BT, are in favour of Option 3. Some of them believe that Option 2 (Reference under the Enterprise Act) should be kept as an option of "last resort". About half of those arguing in favour of Option 3 (in particular UKCTA and the largest altnets) stress the need for Ofcom to be ready and

willing to refer the market to the Competition Commission should Real Equality of Access not be achieved. Others call for such a reference to be used only as an option of last resort and caution of its potential disruptive effects. BT signals a willingness to accept a revised version of Option 3, argues that there is no case for a reference under section 131 of the Enterprise Act and urges Ofcom to accelerate the timeframe for deregulation.

1.6   A few respondents (including Energis among the larger altnets) plead the case for an immediate referral of BT under section 131 of the Enterprise Act. Though views on the scope for deregulation differ, almost all respondents dismiss Option 1 (full deregulation).

Most of BT's competitors urge caution in deregulation in fixed telecoms

1.7   BT urges Ofcom to consider deregulatory moves or at least market reviews in markets which it considers now to be competitive, such as the business voice market. Most altnets, however, argue strongly that premature deregulation will be damaging to the market – they do, however, recognise that deregulation should be an incentive for BT to deliver equality of access. In particular, they argue that a high standard of equality of access needs to be in place in upstream markets before deregulation should be contemplated downstream; including equivalence of input and behavioural change. Many mobile operators urge Ofcom to be more explicitly deregulatory in the mobile market in particular.

1.8   Amongst many consumer groups, associations and individuals, there is a concern about an early move towards deregulation. Many argue that Ofcom should make a clear distinction between regulation designed for fair competition and regulation aimed at consumer protection; and that there is no case for withdrawal of the latter.

Equality of Access

Most respondents agree about the need to enforce equivalence for bottleneck services

1.9   BT broadly accepts the principle of equivalence for enduring economic bottlenecks. However, BT emphasises the difference between equivalence for new bottleneck products which could be built in as these products are developed, and equivalence for legacy products which will be expensive and very time-consuming. Virtually all altnets agree that equivalence of outcomes has not delivered equality of access and therefore argue that only equivalence of inputs will be able to improve the current situation. A number of altnets and service providers argue that as long as BT cannot deliver true equivalence on all fronts, BT's wholesale customers should be entitled to receive financial compensation. Some local infrastructure players (including the cable operators and UK Broadband), argue against the introduction of equivalence to many local access assets, aruging that it will stifle innovation.

A number of proposals are put forward to ensure behavioural and organisational changes by BT

1.10   Although BT challenges Ofcom's allegations of its past malpractices, it puts forward a proposal to create a separate Access Services Division within BT to manage the local access network. BT proposes that the division will have its own incentive structure and that a new Equality of Access board will be created to oversee the delivery of all wholesale products in markets in which it has significant market power (SMP).

1.11 Other respondents had not had the opportunity to see BT's proposals when they submitted their responses. Most altnets and service providers agree that a radical organisational and behavioural change is required of BT, and propose many structural and behavioural changes for BT. Some aspects of the proposals put forward by many altnets and service providers are in line with BT's own proposals. However, typically they also recommend additional requirements such as, for instance, a system of independent audit, the appointment of independent board members, financial liability for non-compliance to a set of agreed KPIs, as well as operational and geographical separation of the new division. Energis is the only altnet to refute that organisational change could ever be sufficient to ensure fair behaviour from BT.

There is strong disagreement about the need for measures to support search and switching by consumers

1.12 Many consumer groups argued that this was one of the most critical issues for Ofcom's review, and used the results of Ofcom's research to highlight the need for measures to improve consumers' ability to search and switch easily between telecoms providers. Though there is some disagreement about what Ofcom's role should be, there is clear consensus among these respondents that there needs to be better access by consumers to clear information about the market, and simplified processes for switching between suppliers. Many consumer groups are do not believe that self-regulatory mechanisms could be sufficient to achieve this.

1.13 Though some telecoms providers recognise that there is a problem among some groups of consumers, the majority are in favour of leaving it to the market to provide information about products and services. Mobile operators argue in particular that Ofcom's research demonstrates that in mobile, there is no issue to address. Some altnets also believe that Ofcom needs to regulate to ensure that consumers can switch easily from one provider to another.

There is agreement in principle for a universal service fund at some point, but many consumer groups urge Ofcom has missed an opportunity to re-consider the scope of universal services

1.14 A large number of respondents agree in principle that when there is greater competition, it would be appropriate to set up a universal service fund. However, respondents differ about when this should be. BT and many consumer organisations welcome the idea and argue for its rapid implementation. Most altnets and service providers argue that it should only be set up once Equality of Access was in place, and competition had developed.

1.15 Many consumer organisations were disappointed that Ofcom's Telecoms Review and Universal Service Review did not give more consideration to extending the scope of universal services. Some, including Ofcom's Advisory Committee on Older and Disabled People argued that universal services should be extended to reception equipment as well as services, and that recipients of universal services should have a choice of supplier. A wide variety of respondents, including many consumer organisations, business organisations such as the Communications Management Association and the Federation of Small Businesses and others argued that broadband should be included as a universal service.

Many also express strong views on geographic-specific regulation, investment, competition in next generation core and access networks, and many other issues

1.16 There was strong disagreement about the need for different regulatory approaches in different geographical areas. BT is broadly in favour. Many altnets were very concerned about this issue, arguing for example that it would be complex to administer, and could create "black holes" where there was no competition. Many respondents from the nations and regions, while welcoming the recognition that there were different competitive problems in different areas, were very concerned about regulation exacerbating a digital divide.

1.17 While BT urges Ofcom to provide the right incentives for investment in its 21st Century Network (21CN), many altnets express significant concerns about the current plan for 21CN and, in particular, the lack of visibility they have concerning BT's plans. Many equipment manufacturers echo this; pointing out how important the access and interconnection arrangements to next generation networks will be for future competition.

1.18 Many business organisations, equipment manufacturers and broadband groups argue how important it is that next generation access networks are rapidly deployed. Many operators point out the scope for current copper and cable infrastructures to be further upgraded. Responses were split over whether Ofcom should forbear from regulating next generation access networks, with many altnets in particular arguing that this would not be appropriate.

1.19 The very wide range of responses we received covered an enormous diversity of issues, some of which we have not been able to capture in this summary. All the non-confidential responses to the Review are available at www.ofcom.org.uk/static/telecoms_review/condoc_phase2r.h
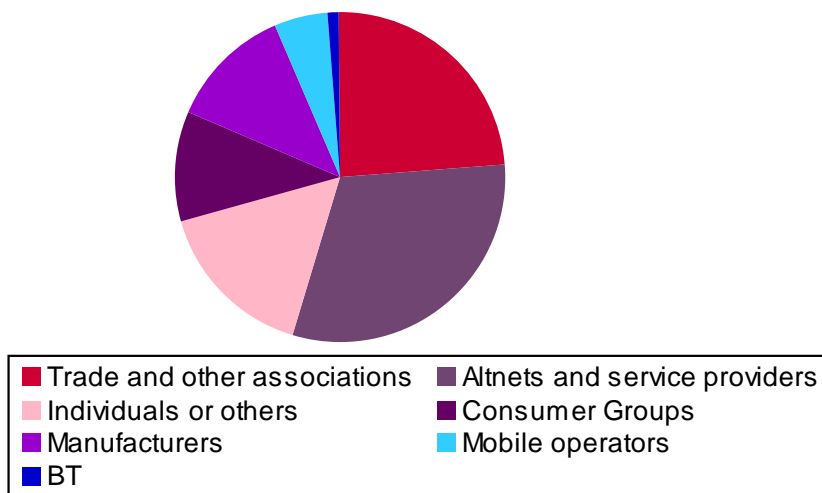
Section 2

Introduction

Document objectives

2.1   Following publication of our Phase 2 consultation document in November 2004, we have received around 100 responses from a broad range of stakeholders, including telecoms operators, service providers, consumer and business groups, associations, regional bodies, manufacturers and private individuals. Given the volume of responses, we have produced this summary of all non-confidential responses submitted to Ofcom. We hope this will facilitate further debate about the issues in the Telecoms Review, by allowing people easy access to the views expressed by other respondents.

2.2   Below we provide a breakdown of the responses submitted by principal stakeholder grouping.

Figure 1: Breakdown of respondents by type of organisation

Legend:
- Trade and other associations
- Altnets and service providers
- Individuals or others
- Consumer Groups
- Manufacturers
- Mobile operators
- BT

2.3   In preparing this summary document, we concluded that it would be more valuable to provide a synthesis of responses by broad issue, rather than for each of the 20 questions raised in the consultation document. The key areas we cover include:

- views on the overriding principles of the strategic review and what Ofcom should do next;

- views on the three options presented by Ofcom;

- specific points made on each the three options (deregulation, reference under the Enterprise Act and equivalence;

- consumer and citizen issues; and

- other issues, encompassing broadband, geographic markets, next generation networks and mobile termination.

2.4   We hope that respondents will understand that in producing this summary, we have had to simplify their arguments, in some cases to generalise about categories of respondents, and in many cases not to include in particular points that individual respondents have made.

Section 3

Overriding principles

Overview

3.1   In the Phase 2 Consultation (paragraph 5.3), Ofcom proposed seven principles for telecoms regulatory policy. They are that Ofcom should:

   3.1.1   promote competition at the deepest levels of infrastructure where it will be effective and sustainable

   3.1.2   focus regulation to deliver equality of access beyond those levels;

   3.1.3   as soon as competitive conditions allow, withdraw from regulation at other levels;

   3.1.4   promote a favourable climate for efficient and timely investment and stimulate innovation, in particular by ensuring a consistent and transparent regulatory approach;

   3.1.5   accommodate varying regulatory solutions for different products and where appropriate different geographies;

   3.1.6   create scope for market entry that could, over time, remove economic bottlenecks; and

   3.1.7   in the wider communications value chain, unless there are enduring bottlenecks, adopt light-touch economic regulation based on competition law and the promotion of interoperability.

3.2   A large majority of respondents agreed with these principles, although some divergence of opinion exists about their application. A number of respondents identified a few shortcomings in these principles, and some argued for greater focus on some of the principles versus others.

3.3   Below we present the views on the proposed regulatory principles, organised by category of respondent. Many of the issues raised in this section are discussed in more detail later in this summary.

BT argues that Ofcom does not place sufficient emphasis on deregulation, regulatory forbearance, consistency and a "bias towards investment"

3.4   BT expressed overall support for the seven regulatory principles but argues for amendments that would lead to greater clarity. It makes four specific points:

   - Ofcom needs to make its commitment to deregulation (Principle 3) clearer. BT suggests that Principle 3 should be amended to reflect that there is an active agenda for achieving deregulation.

   - Ofcom should apply the principle of forbearance for emerging markets such as next generation access, as the risk of inappropriate regulation would be severe. BT suggests an amendment to the fifth principle which would recognise the possibility of forbearance in new and emerging markets.

- Ofcom's commitment to ensure a "consistent and transparent regulatory" approach does not seem consistent with some of Ofcom's ongoing initiatives such as the proposed changes on the cost of copper which BT argues is at odds with the principle of creating the right environment to encourage investment.

- The need for a "new regulatory settlement" needs to be backed by an implementation plan from Ofcom that demonstrates the regulatory commitments towards achieving the new settlement. BT proposes a number of measures that should be part of the regulatory settlement, including, amongst others, the process by which deregulation will take place as circumstances change.

Altnets and service providers voice broad agreement with the regulatory principles but argue for a clear roadmap for achieving these

3.5 Most of these respondents broadly agree with the regulatory principles set out by Ofcom. A number of respondents, though, argue that practical implementation without a clear roadmap will be difficult to achieve. The UK Competitive Telecoms Association (UKCTA), which has acted as spokesman on issues of consensus on behalf of a number of altnets and service providers, cautions Ofcom about the pitfalls of a theoretical debate on equality of access without clear and agreed timelines for BT: *"Industry as a whole cannot afford to sit through months of talks while competition continues to be harmed through the marked lack of equality of access on BT's key bottleneck wholesale products".*

3.6 France Telecom speaks for many players in agreeing that ex ante regulation should be focused on enduring bottlenecks, while other areas are best regulated on the basis of ex post application of competition law. There is some divergence of opinion amongst respondents, though, as to what constitutes an enduring bottleneck. UKCTA argues for an empirical exercise to determine this. Some service providers point out Ofcom's duty to impose remedies in markets wherever it finds there to be significant market power (SMP), not just where there is an enduring bottleneck.

3.7 Most altnets and service providers voice support for the principle of regulation encouraging competition at the deepest level of infrastructure where it will be effective and sustainable. However, many point out that this level in the network is different in different geographies. In particular, in broadband, they argue that LLU will not be viable in all places. A small number of operators, including Thus and Viatel, have expressed a concern that Ofcom is too biased towards LLU when there are bottlenecks higher up the value chain, such as for example in Wholesale Line Rental (WLR) and bitstream access. The CWU and Connect argue that Ofcom's emphasis on LLU neglects the interests the proportion of the population not covered by the largest exchanges where, they argue, LLU is uneconomic. Viatel argues that Ofcom appears to be favouring a regulatory environment that supports a few large infrastructure-based players but that, ultimately, there is a risk that service-based competition may not be viable, leading to damaging consequences for end users.

3.8 Most operators believe that geographic de-averaging is premature, will be complex to implement and potentially dangerous as it offers scope for BT to rebalance its prices in some areas. This is discussed in more detail later in this summary. Your Communications is one notable exception, as it believes that BT's prices within its own footprint are subsidised by profits made in more densely populated areas, resulting therefore, in unfair competition.

3.9 Finally, a number of respondents emphasise the problems of an industry structure where there is much fragmented competition, with many sub-scale players,

Alternative access infrastructure players[1] disagree that local access is an enduring bottleneck, and argue that treating it as such will discourage true infrastructure based competition

3.10 UK Broadband makes the point that infrastructure based competition is by far the best means for promoting competition*: "Infrastructure investment and network competition, instead of resale and services competition, is the most significant element of progressive liberalisation of the telecommunications market".* Both NTL and Telewest share this view and insist that infrastructure based competition will drive innovation and allow for deregulation in future.

3.11 The three players refute the suggestion that access is an economic bottleneck which is not contestable. Indeed, they argue that by defining it and regulating it as such, the principle of access being an economic bottleneck becomes self-fulfilling. NTL makes a point on the need for Ofcom to provide regulatory certainty through the investment cycle which, in the case of access networks, is a long timeframe. It calls for Ofcom to state explicitly the market structure it is trying to achieve.

Mobile operators suggest that Ofcom needs to allow for full deregulation in mobile

3.12 Many mobile operators make the observation that Ofcom is right in focusing the Strategic Review on the fixed market but would like Ofcom to be more explicitly deregulatory in the mobile market. They argue for Ofcom to develop a strategy designed to lead to full regulatory withdrawal from mobile markets in due course.

Consumer groups argue for Ofcom to take a more balanced view of both the supply and demand side of the market

3.13 The general view from many consumer groups is that Ofcom has not done enough to protect the interests of all types of consumer. Groups including the Royal National Institute for the Blind, the Royal National Institute for the Deaf and the Citizens Advice Bureau, expressed concerns about the way the consultation did not give enough attention to the needs of the most vulnerable groups of consumers, whether this be consumers with special needs or low income groups.

3.14 Many of the consumer groups believe that the consultation is very much supply-side oriented focusing on the technical issues around the way industry players access each others' networks rather than how well the telecoms industry delivers to consumers and citizens. For example, some highlight that Ofcom's proposed regulatory principles do not contain a single mention of citizens and consumers.

3.15 The Ofcom Consumer Panel speaks for many, in making the point that the principle of "real equality of access" should not only be applied to the industry but also to consumers. It thinks that the fact that the Phase 2 document considers consumer issues at the end is symptomatic of the low priority that these issues have received.

3.16 Finally, a number of these respondents argue that it is inappropriate for Ofcom's universal services review to be held in parallel to the Telecoms Review; they argue that this issue should be an integral part of the Telecoms Review.

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[1] We include in this category the cable-operators and UK Broadband, the wireless broadband operator

Manufacturers: focus on principle 7 and the need for interoperability

3.17 Telecoms equipment manufacturers mostly agree with the principles set by Ofcom but focus in particular on those relating to next generation core networks (NGNs) and Next Generation Access. In particular, they highlight the need for interoperability in the context of NGNs, and point out the need to address this at the design stage. Many emphasise the need for regulation to encourage investment in next generation access networks.

3.18 National and regional groups as well as industry associations voice overall agreement with the regulatory principles but highlight a few specific shortcomings

3.19 A few industry associations (e.g. the British Music Group and the Confederation of British Industry) expressed their disappointment about the lack of focus of the consultation on the wider value chain in general and on content in particular.

3.20 A number of regional interest groups highlight their concerns on what they see as a widening digital divide, and argue that a geographic approach to regulation might actually exacerbate rather than address this issue, as it would lead to increased prices for telecoms services in rural areas. This issue is addressed in more detail later in this summary.

Views on the process of the Telecoms Review

4.1   A number of respondents outline specific key next steps that Ofcom should take as a follow-up to the consultation. These cover a range of issues. Below we have summarised the themes that have been raised by a number of players.

4.2   **Need for a clear and practical equivalence roadmap**: while most telecoms operators welcome Ofcom's proposals on Real Equality of Access, many are also sceptical about BT's willingness to voluntarily deliver this. Many respondents amongst this group have requested that Ofcom define a clear roadmap for its introduction, with specific timelines and milestones. They argue for specific financial penalties to be levied on BT in the event of non-compliance and invite Ofcom to give greater clarity on how it proposes to apply the threat of a reference under the Enterprise Act.

4.3   **Important for Ofcom to present a clear roadmap on the process by which deregulation will take place as circumstances change:** This specific point is raised by BT which urges Ofcom to be more explicit on how it proposes to implement deregulation.

4.4   **Importance of a co-ordinated approach to Ofcom consultations**: a number of respondents voice their concern as to why Ofcom is holding parallel consultations on, for example, the cost of copper, next generation networks and universal services, at the same time as the Telecoms Review. There is a general concern that duplication of efforts on these topics could lead to some oversight and dilution of these issues. Consequently, Ofcom is urged to provide more clarity as to how it proposes to deal with industry views expressed in such parallel consultations.

4.5   **Essential that Ofcom does not allow itself to be distracted from important shorter term issues:** some respondents argue that while Ofcom's principles and long term goals are laudable, Ofcom should not be diverted from short and medium term priorities aimed at promoting competition, such as the rapid implementation of fit-for-purpose wholesale products (e.g. WLR).

4.6   **Requirement for more constructive industry consultation on 21CN**: a number of respondents urge Ofcom to facilitate further engagement from BT with the rest of the industry on the terms of access to its Next Generation Network. The CWU and Connect argue that whilst equivalence is important it needs to be viewed in the context of allowing BT the returns from investment and innovation, and, they posit, from being able to benefit from vertical integration.

4.7   **Need for consultation on geographic regulation**: A number of respondents, including altnets and regional bodies, urge Ofcom to consult specifically on the issue of tailoring regulation to particular geographic areas before introducing any regulation of this nature.

4.8   **Important to launch a debate on ways of lowering switching costs: while** most respondents do not believe that switching costs faced by consumers and businesses should be reduced to nil, both service providers and consumer groups think that it would be beneficial for Ofcom to engage with the industry and consumer groups on options for lowering switching costs.

Section 5

Views on the three options

Overview

5.1 In its Phase 2 consultation document, Ofcom presented three possible options for a future regulatory approach:

- **Option 1**: Deregulation: remove sector-specific regulation and rely on using the Competition Act to address any remaining problems.

- **Option 2**: Reference under the Enterprise Act: assess whether any feature or combination of features of a market prevented, restricted or distorted competition in a way which requires remedies going beyond Ofcom's powers under the Communications Act and the Competition Act; and consider making a reference under section 131.

- **Option 3**: Real Equality of Access: focus regulation on enduring economic bottlenecks, and tackle the problem of inequality of access head-on.

5.2 We have synthesised the responses to the three options in Figure 2. Amongst the respondents, more than half expressed a clear view of their preference over one of the options, with the remainder not expressing a specific opinion. Of those who expressed a view on this question, the vast majority (90%), including BT, are broadly in favour of Option 3. Within the group favouring Option 3 there are two distinct subgroups which express diverging points of view on the circumstances in which they consider that it would be appropriate to make a reference under the Enterprise Act. The first sub-group, including in particular UKCTA and the largest altnets, argues that Ofcom should be willing and ready to make a reference should Real Equality of Access not be achieved. The second sub-group, including some service providers, and some telecoms players without extensive national infrastructure, many equipment manufacturers and others, argues that a reference should be made only as a very resort, or in some cases in no circumstances at all. This group cautions of the potential disruptive effects of such an action.

5.3 A few respondents (Energis, Gamma Telecom and a private individual) argued the case for an immediate referral of BT under section 131 of the Enterprise Act.

5.4 The general view expressed on deregulation (Option 1) by almost all respondents is that the market is not yet ready for a move to full deregulation.

Figure 2: Views of the respondents on the 3 options
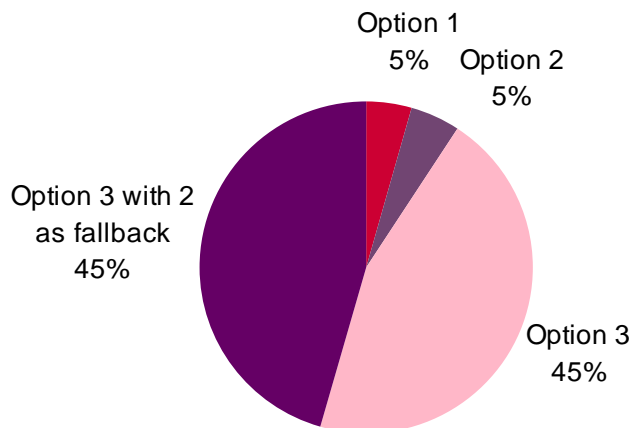
BT states it is willing to support a variation of Option 3 and expresses doubts on the grounds and prospects for Option 2

5.5   BT argues that Ofcom's power to impose "real equality of access" is limited. It argues that "equivalence" is not a defined legal term and is not included in the list of remedies available to Ofcom under the 2003 Communications Act, which empowers Ofcom to impose remedies to address undue discrimination. BT also considers that the "problem of inequality of access" has not been accurately or convincingly described in the Phase 2 document.

5.6   However, BT accepts the need for equivalence of access to core enduring bottlenecks, and puts forward a number of proposals to address issues of behaviour and governance.

5.7   Regarding Option 2, BT believes that there is currently no justification for a reference under section 131 of the Enterprise Act. BT also signalled that it was ready to contemplate an Enterprise Act investigation although it is convinced that this avenue will be difficult for many reasons. BT would like to understand what further investigation Ofcom intends to undertake prior to deciding whether or not to make a reference under the Enterprise Act. BT expresses doubts that Ofcom has a case to put together a pre-condition for a reference. BT argues that a reference will be "costly and burdensome", "very lengthy" and the results of the reference process and advantages of structural separation are "uncertain".

5.8   Finally, on Option 1, BT urges Ofcom to accelerate the timescales for deregulation. BT believes that it is incumbent on Ofcom to seek to deregulate wherever possible, and consequently, deregulation should not be regarded as an option but an obligation. It thinks that Ofcom should generally rely on ex post competition law and use ex ante regulation as a last resort. BT believes that the consultation is unduly pessimistic on the effectiveness of competition law.

The majority of altnets and service providers support Option 3 but urge Ofcom to consider Option 2 in the event of Option 3 failing to deliver

5.9   The majority of altnets and service providers believe Option 3 is the best approach. An immediate reference under the Enterprise Act is viewed by most as a cumbersome

way to achieve real competition: it would be disruptive for the market as a whole, would take long to implement and there would be no guarantee of success.

5.10 However, there is also a consensus that reference under the Enterprise Act should be given serious consideration. There is some variation, however, amongst respondents in this category as to the circumstances under which a reference under the Enterprise Act should be made. Most of the altnets support the view of UKCTA that Ofcom should keep the pressure on BT, and make a reference under the Enterprise Act should BT fail to show evidence of a move towards "real equality of access". Most altnets argue that real equality of access will only be achieved if Ofcom manages to set unequivocal definitions, milestones and timelines to which BT will publicly agree. IDT proposed a solution which would mix Option 3 and Option 2; suggesting that Ofcom should put on hold a reference under the Enterprise Act for 6 months and if BT can demonstrate its ability to deliver equality of access during this period, then it should be given another six months with a view to achieving "true equality of access" by the end of this period.

5.11 However, some altnets adopt a more aggressive view on the recourse to Option 2. C&W, for instance, raises the point that the Enterprise Act may be the only way forward if an agreement cannot be swiftly reached with BT: *"Although an Enterprise Act reference is a second best option, nevertheless it is superior to an inadequate or non-compliant implementation of access by a resistant BT".* Tele2 believes that there would be a significant advantage in opening an Enterprise Act investigation in parallel with trying to make Option 3 work.

5.12 Energis and Gamma Telecom take a more radical approach than the other respondents in this category, arguing that reference under the Enterprise Act and the subsequent separation of BT has already become the last and only option to turn around the current situation. In particular, Energis believes that the key issue resides in BT's vertical integration, that while this remains equality of access will not be achieved. It argues that the practical problems of achieving BT's separation are surmountable.

5.13 Regarding Option 1, there is a clear agreement among Altnets and Service Providers that deregulation in the market is premature. Most fear that the deregulation agenda proposed by Ofcom under Option 3 is moving too fast. A clear consensus argues for the necessity of keeping ex ante regulation in place as well as ex post competition and the application of competition law. As highlighted by Carphone Warehouse, many argue that competition law has usually proved to be inefficient in solving competition issues in telecoms, particularly because investigations are long and often subject to appeal.

Alternative access infrastructure players have concerns about the detailed application of Equality of Access

5.14 As highlighted earlier in this document, the local access infrastructure players have diverging views from Ofcom on the key principles, the focus on equivalence and whether local access is an enduring economic bottleneck. As a consequence their views on the three options differ significantly from other industry players. NTL and Telewest are broadly in favour of Option 3 but have significant concerns on the definitions and consequences of true equality of access. Telewest expressed concerns about an Enterprise Act investigation, stating that it cannot foresee any circumstance where Option 2 would be appropriate. NTL supports the UKCTA view on Option 2, and suggests that there could be grounds for BT's separation.

5.15 UK Broadband is one of the few respondents to put forward a case substantially in support of Option 1. It argues that Ofcom's overriding priority should be to encourage infrastructure-based competition. It argues that there should be unbundling only where the competition law test of an essential facility is met. Therefore, it opposes the unbundling of BT's assets further back in the network, and believes that unbundling should only be seen as a temporary solution.

Mobile Operators

5.16 In general, mobile operators expressed few detailed opinions on the three options, except to voice their desire to see Ofcom become more explicitly deregulatory in the mobile market.

Manufacturers and broadband campaigns support Option 3

5.17 Manufacturers tend to agree that out of the three options, "Option 3, 'real equality of access', is the only viable way forward", as Nortel put it. Most of this group is against a reference under the Enterprise Act. Siemens argues, for example, that there is not sufficient evidence of a deliberate policy by BT to "prevent, restrict or distort" competition.

Amongst other respondents, most broadly support Option 3 – though there are exceptions

5.18 Not all respondents expressed a strong view on their preferred option. Of those who expressed an opinion, most voiced support for Option 3. Business user groups including the Confederation of British Industry, the Federation of Small Business and the Communications Management Association, stated that they were in favour of Option 3. The Communications Management Association (CMA) pointed out that the majority of their members were in favour of Option 3, with only a few showing a preference for the other two options.

5.19 The Broadband Stakeholders Group (BSG) advocates a general de-regulatory stance. Whilst it supports Ofcom's belief that the current regulatory approach hasn't delivered adequate competition in the fixed network market, it states that further intervention could undermine investment. It believes that *"the balance should be tilted towards the deregulatory option with more emphasis on behavioural regulation of SMP players"*.

5.20 Consumer groups were mostly concerned about the dangers of Option 1 and the move to a fully deregulated telecom environment. The Citizens Advice Bureau (CAB), for instance, argues that regulation is required to ensure good customer service and eliminate rogue practices by telecoms players. In addition, the CAB states that it is naïve to assume that competition can fill the gap in terms of consumer interests and that "light touch" regulation fails to protect consumers.

5.21 Individual respondents had a variety of views on the three options. The majority supported the idea of Option 3, with many also arguing that a reference under the Enterprise Act should be kept as a threat to BT. Dr Kaishu Thai put forward the concept of an ultimatum of 18-24 months to be given to BT to fulfil equality of access, with a reference under the Enterprise Act if it fails. Bob Franklin and Len Hawkes suggested a fourth option, involving a voluntary restructuring of BT.

Section 6

Deregulation

Overview

6.1 While BT urges Ofcom to consider rapid deregulation in a number of markets, most altnets believe that premature deregulation will be damaging to competition. The altnets do, however, accept the importance of deregulation as an incentive for BT to deliver equality of access. The mobile operators ask Ofcom to be more explicitly deregulatory in the mobile market. Amongst consumer groups, associations and individuals, there is a clear concern about a premature move towards deregulation. Many in this group urge Ofcom to make a clear distinction between regulation designed for fair competition and regulation aimed at consumer protection.

BT urges Ofcom to fulfil its commitment to deregulation

6.2 BT urges Ofcom to accelerate the timescales for deregulation. It reminds Ofcom of its duty to carry out new market reviews at regular intervals with a requirement to withdraw regulation where markets are effectively competitive.

6.3 BT also presses for additional deregulatory moves in a number of markets where Ofcom has either ruled out deregulation or argued that the evidence for deregulation is not yet compelling. It considers that a market review is needed in the business voice market, given the increasing level of competition. It also urges Ofcom to consider the withdrawal of ex ante regulation ahead of the market review of what it regards as the "highly competitive" large business voice market.

6.4 BT believes that Ofcom should rely on ex post competition law and only use ex ante regulation as a last resort. This view contrasts with that expressed by many other respondents. As shown in Figure 3, the majority of respondents believe that, given the current competitive environment, ex ante regulation should prevail with a very cautious use of ex post competition law in markets that have clearly become competitive.

Figure 3: Respondents' general preferences in response to Ofcom's question: "Where and to what extent should Ofcom rely on ex post competition law rather than ex ante regulatory conditions?"
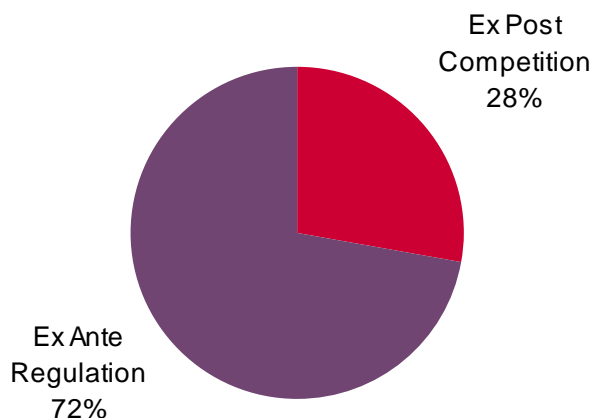
6.5 BT welcomes the moves of Ofcom to deregulate in the markets mentioned in the Phase 2 consultation. BT agrees with the approach to deregulating the voice market but states that it would expect more clarity on the timescales and the scope. It also believes that fixed and mobile should already be considered as a single voice market. It agrees with the need for a review of regulation of the voice market in 2005 but challenges the link between deregulation and the delivery by BT of a "fit-for-purpose" WLR product, arguing that no such pre requisite should be placed for deregulation in the business sector. BT believes that market conditions justify deregulation of conveyance markets and wholesale IDD.

Altnets and service providers argue that deregulation is premature and any move in this direction should be contingent upon BT's delivery of "Real Equality of Access"

6.6 Altnets in particular are cautious about Ofcom's proposal to deregulate parts of the network that are not enduring economic bottlenecks. Bulldog speaks for many in stating that premature deregulation will be damaging to the market. Overall, there is a clear stance against granting deregulation too early without significant evidence of true competition. As Your Communications put it, *"the proof must be in the measurable actions, not the words".* Viatel makes the point in stating that it is *"hard to envisage a time, in respect of most of BT's wholesale services, when the competitive conditions will allow withdrawal from regulation".*

6.7 However, this group of respondents mostly states that they also believe that deregulation will play a role as an incentive for BT to deliver equality of access. Carphone Warehouse proposes providing BT with a clear roadmap for deregulation to create incentives for BT to implement equivalence. However, respondents also agree that the hurdle imposed on BT should be high and include both full equivalence of inputs for upstream products and organisational and behavioural change by BT.

6.8 Concerning deregulation in specific markets, Caudwell and Tiscali are representative of a number of respondents in suggesting that deregulation should only take place in downstream markets once upstream issues are resolved.

6.9 In the voice market, most altnets are not against deregulation, provided that BT is able to deliver true equivalence on its WLR and CPS products. ISPA UK calls for a market review of the voice markets in 2005 (as well as the wholesale IDD and conveyance markets) in order to assess whether these markets still need to be regulated or not. Almost all altnets believe that IDD is now a sufficiently competitive market to be deregulated.

6.10 Regarding business voice services, most altnets do not believe that the competitive situation has significantly evolved since the last Ofcom market review, and again believe that BT will need to provide "fit-for-purpose" wholesale products in this market before regulation can be removed.

6.11 Some, such as Tele 2, argued that Ofcom should not withdraw from regulating call conveyance markets until BT offers a commercially viable wholesale alternative. There was also a general agreement that Ofcom should be cautious in removing regulation from Indirect Access.

6.12 In general, this group believes that the right approach for Ofcom is ex ante regulation unless there is unequivocal evidence of competition in the market.

Local access infrastructure players show a more favourable attitude towards deregulation than altnets

6.13 Both NTL and Telewest showed less caution about deregulation of the retail markets than the altnets. UK Broadband voiced its support for a significant reduction in regulation, referring to the EU Framework Directive that Ofcom should only intervene where there are proven enduring economic bottlenecks and that, in other cases, regulatory intervention should carry the burden of proof.

Mobile players

6.14 As mentioned above, mobile players assert their view that Ofcom needs to be far more explicitly deregulatory in the mobile market. O2 argues, for example, that "a clear and coherent strategic deregulatory roadmap in respect of mobile is needed".

Other respondents

6.15 The majority of respondents from consumer groups believe that the market is not ready for deregulation. They are particularly cautious about deregulation even in the longer term, regardless of BT's ability to provide true equality of access or not. Many in this group believe Ofcom is over-reliant on competition as a means of protecting consumers. The Royal National Institute for the Blind points out that free market outcomes often do not deliver good outcomes for non-mainstream customers. The National Consumer Council (NCC) also points out that unfettered competition can lead to slamming, poor consumer information, disconnection of vulnerable customers, poor debt management, and unduly burdensome switching procedures.

6.16 The NCC also introduces a distinction between regulation designed for fair competition and regulation for consumer protection. It comments that *"regulation for fair competition and regulation for consumer protection are qualitatively different. Withdrawal of the first does not always imply withdrawal of the second"*.

Equality of Access

Overview

7.1   In the Phase 2 consultation document, Ofcom argued that Real Equality of Access would involve both behavioural and organisational change by BT, and equivalence at a product level. We defined two types of product level equivalence: equivalence of inputs, where BT's wholesale customers had access to exactly the same products, at the same price and using the same processes as BT's own divisions; and equivalence of outcome, where the products might not be identical but were comparable.

7.2   BT broadly accepts the need of equivalence for enduring economic bottlenecks. However, it states that equivalence of input on legacy products will be time-consuming to achieve. Virtually all altnets agree that equivalence of outcomes, as it has been adopted to date, has not delivered equality of access and argue that only equivalence of inputs will be able to improve the current situation. A few altnets and service providers argue that as long as BT cannot deliver true equivalence on all fronts, BT's wholesale customers should be entitled to receive financial compensation. Alternative access infrastructure players (cable operators and UK Broadband), argue against the concept of equivalence to many local loop assets, claiming that it will stifle innovation.

BT supports equivalence for enduring economic bottlenecks

7.3   BT broadly accepts the need for equivalence for enduring economic bottlenecks and accepts, *"as part of an overall new regulatory settlement, a commitment to deliver an agreed form of equality of access"*. For legacy products, BT argues that equivalence of input will take time and require substantial new investment. Therefore, BT believes that equivalence should only apply immediately to new products. BT is, however, willing to move towards input equivalence of legacy products, including WLR, LLU and broadband leased lines, with implementation starting in 2006 and completing by 2010.

7.4   BT supports equivalence of outcomes over equivalence of inputs, but indicates that in the context of its imminent programme of systems renewal, it is willing – as part of a new regulatory settlement – to deliver equivalence of inputs on a defined set of enduring economic bottlenecks. BT also commits to improve WLR processes and to improve the margin between WLR and retail line rental.

7.5   As described in Figure 4 below, the overwhelming majority of respondents were in favour of equivalence of inputs over equivalence of outcomes. Other than BT, only four other respondents favour equivalence of outcomes over equivalence of inputs and a further three argue that equivalence of inputs would be preferable only if it did not place an unrealistic cost burden on BT.

Figure 4: Answers[2] to Ofcom's question: "Do you agree that equivalence of inputs can deliver more effective equality than application of equivalence of outcomes?"
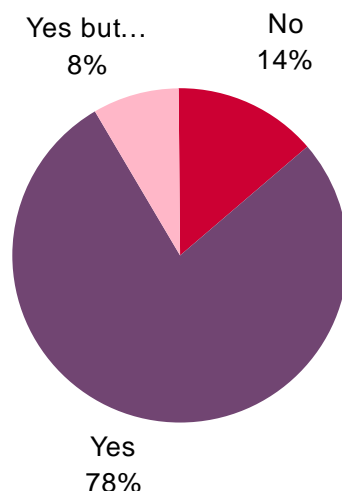
7.6 In the case of "associated products", in particular migration products, BT contests that, since it does not use these products itself, there is no case for enforcing the principle of equality. BT does, however, state that there will be opportunities for discussion with its customers on this issue, when BT begins to migrate its own downstream services to new platforms.

Altnets and service providers assert that equivalence is needed urgently at a product, price and process level

7.7 Virtually all altnets and service providers agree that equivalence of outcomes has not delivered equality of access and argue that only equivalence of inputs will be able to improve the current situation.

7.8 Equivalence is a mix of three elements comprising products, processes and prices. Bulldog makes the point that while pricing equivalence can be delivered more rapidly, product and process equivalence will take longer to implement.

7.9 Given the potential complexity of issues relating to product and process equivalence, UKCTA argues in tune with a number of players that, as long as BT cannot deliver true equivalence on all fronts, BT's wholesale customers should be entitled to financial compensation, possibly in the form of price reductions.

7.10 Many altnets raise the issue of equivalence for WLR; in terms of pricing, product and processes. Most altnets argue that even though they have experienced a decrease in WLR rates, they wish to see BT lower its wholesale prices further and increase the margin between line rental and WLR, and that this price decrease should be a pre requisite for equivalence for WLR. They make the case for a fit-for-purpose WLR product, which they argue will also require some fundamental changes in terms of processes. Blueridge provides a description of some of the issues facing WLR currently which include "delays on all-fronts" in the roll-out of the WLR contract, "unnecessarily onerous forecasting requirements" and difficulty in extracting information from BT.

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[2] We only took into account responses which addressed this question

7.11 The Association of Communication Service Providers contests Ofcom's view that CPS is now a level playing field.

7.12 This group of respondents emphasises in particular that migration services are a key element in their businesses and that BT has no incentives to develop or improve these. Centrica, for example, supports the idea that migration issues should be solved through contractual SLAs, regulatory KPIs and backed by financial penalties by BT for non-delivery.

7.13 Many respondents conclude that equivalence should be provided for all "underlying building blocks" of the wholesale offers, as well as other products "lower and higher" in the value chain. Priority should be given for specific wholesale products (including LLU, Datastream, wholesale leased lines and WLR), and many altnets support the principle of equivalence for basic building blocks such as dark fibre. Although a small number of altnets state the need for equivalence for PPCs, but more argue that instead, a dark fibre wholesale product is required.

7.14 A number of altnets and service providers point out the disadvantage they suffer in not having access to BT's access databases, and argue that equivalence should be extended also to these.

Alternative access infrastructure players are sceptical about the principle of equivalence for many local access products

7.15 As noted before, all the alternative access infrastructure players who responded are sceptical about the notion of equivalence. Telewest argues that equivalence will lead to innovation being stifled as everyone is using the same basic inputs. It suggests that equivalence should be used only for simple interconnection products. NTL suggests that equivalence should only be a solution in the case of a natural monopoly assets, and suggests that some ducts might be the only local network asset to which this might apply.

Other respondents who voiced broad support for equality of access, highlight some additional concerns

7.16 A number of consumer groups, trade associations and other respondents raised some specific concerns about the application of equality of access.

7.17 Although the Ofcom Consumer Panel agrees that real equality of access should be the way forward for the industry, it argues for the need for equality to deliver positive results for consumers. It is, therefore, not prepared to accept that genuine equivalence can be made to work without a clear and measurable framework against which to judge its success. As mentioned in Section 3, the Ofcom Consumer Panel asserted that real equality of access should be applied not only to the supply side but also to the demand side.

7.18 The Communications Workers Union (CWU) makes the point that achieving equivalence will require a lot of effort from BT (systems development) and that BT needs to be given some time to achieve this. It argues that equivalence also has to be achieved in a way that still provides BT with incentives to invest in its network. It argues that equality of access should be limited to enduring economic bottlenecks, not all services. CWU makes the same point as BT that, while equivalence of inputs can be achieved for new services, in the case of legacy wholesale services, the focus should be on equivalence of outcomes. It thinks that it would be generally

inappropriate to use input-based equivalence where this would entail additional costs and delays.

Behavioural and organisational changes

Overview

7.19 Although BT challenges Ofcom's allegations of past malpractices, it outlines proposals for the creation of a new Access Services Division, a separate structure within BT managing the local access network. The division would have its own incentive structure. BT also proposes creating a new Equality of Access board, with overview responsibility for the delivery of all SMP wholesale products. Altnets are unanimous in their view that a radical organisational and behavioural change is required and make a number of proposals on how this could be achieved. As Energis is the only respondent amongst the altnets who argues for a reference under the Enterprise Act, it thinks that no behavioural or organisational measures are likely to be effective, short of the separation of BT into companies with different ownership.

BT proposes to establish a separate Access Services Division as a means of achieving equality of access

7.20 Even though BT made many proposals in its response to improve the current situation, at the centre of its argument is a denial of previous malpractices. First BT points out to the very limited past record of enforcement of competition law actions against it. BT challenges Ofcom to provide real evidence instead of hearsay evidence of abuses of BT's market dominance. Furthermore, BT uses Ofcom's own research to produce evidence that UK telecoms markets compare favourably on certain key indices.

7.21 BT does, however, put forward a proposal to address the issue of the access bottleneck. BT proposes to create a new Access Services Division (ASD), to include the genuinely enduring economic bottleneck of the 'last mile' between the customer and the local exchange (strictly speaking, the main distribution frame, or MDF, in the local exchange). The ASD would not include backhaul, and would not house services with any 'managed' element going beyond the MDF, such as Wholesale Line Rental. It is proposed that the ASD would be a separate entity within BT with its own incentive structure based on delivery of KPIs in relation to access services.

7.22 BT also proposes creating a new Equality of Access Board (EAB), which would include two independent members appointed in consultation with Ofcom – one of whom could be an Ofcom board member. The EAB would have oversight of the delivery of all SMP wholesale products, including those not included within the Access Services Division. In this way, BT is seeking to address the problem of there being markets in addition to economic bottlenecks in which it nonetheless has significant market power.

Altnets and service providers call for a significant change of behaviour from BT

7.23 Many altnets and service providers described in some detail what they see as evidence of past misconduct by BT. Variously, they referred to:

- misuse of customer information obtained from altnets and service providers;
- bundling of SMP and non-SMP services;
- unacceptable timescales; and
- slow product development.

7.24 Many of these respondents argue that although each incident of misconduct by BT is sometimes small, they argue that the cumulative effect of BT's current behaviour towards competitors has had a significant impact on altnets' and service providers' ability to compete effectively.

7.25 Kingston makes the point that it is difficult to collect concrete evidence on BT examples of misconduct, as this often requires the end customer to formally submit evidence, which customers are generally reluctant to do. This results in a vicious circle, whereby without the necessary evidence, Ofcom cannot instigate investigations. Consequently, Kingston would like Ofcom to initiate an "own initiative" investigation into BT anti-competitive practices. Specific examples Kingston refers to include concerns over aggressive BT behaviour in the corporate market, including pricing off list, bundling of SMP and non SMP services, misuse of information gained from altnets and claims that BT has exclusive supplier rights in public sector.

7.26 Viatel gives a specific example of what it implies is evidence of unfair treatment by BT vis a vis new entrants, in that BT requires cash deposits, thus creating an "unreasonable" barrier to entry. Viatel speaks for a number of altnets in stating that: "BT should be more energetic, pro-active and responsive to their wholesale customers". Your Communications further endorses this point by arguing that BT's relationship with other service providers should become more of a partner/supplier relationship as is the case in other markets, and that for this to be achieved major behavioural change within BT needs to happen.

7.27 Having argued that there have been a number of incidents of anti-competitive behaviour by BT, several altnets and service providers provide views on what behavioural changes by BT would be required to ensure fairer treatment of wholesale customers. UKCTA, on behalf of several altnets and service providers, states that a "radical organisational and behavioural change" is required.

7.28 Because all the responses were due in at the same time, no respondent had an opportunity to comment on BT's proposals when they submitted their own responses. However, a number of altnets and service providers discussed what changes by BT they thought would be necessary.

7.29 The majority of respondents in this group endorse the idea of a separate Access Division and the need for this to be independent. There are variations in views as to the extent to which a new Access organisation should be a separate company from BT Group (which was the view put forward by UKCTA and endorsed by others such as C&W), or simply a separate operating division within BT Group. Carphone Warehouse, for example, supports the idea that BT must create one or several separate internal divisions with employees' incentives based on the commercial success of the divisions in question. ISPA argues for a physically separate location of the wholesale arm of BT, with a different line of reporting to the BT board as a means of minimising conflicts of interest between BT Retail and BT Wholesale.

7.30 Most altnets and service providers agree that the new Access division should include only local loop assets. While most argue that backhaul is also a bottleneck, many envisage this being provided by an SMP division within BT Wholesale, separated by the rest of BT Wholesale by effective Chinese Walls.

7.31 In terms of which access products should be included in the new Access division, again there is some divergence of opinion, although most agree that LLU should play centre stage. C&W, for example, envisages that this division will focus on basic access

to unbundled loops and dark fibre, with CPS and WLR being provided by BT Wholesale.

7.32 Respondents in this category make some suggestions as to how effective governance of this separate Access Division can be ensured. Suggested measures include:

- appointing independent board members to oversee the effective functioning of the Access Division and ensuring that this division has its own direct reporting line to the BT Group board;

- bringing in new management from outside BT to head up the Access Division and implement reforms;

- putting in place Chinese Walls to ensure that there is no inappropriate exchange of information with other BT divisions that would result in BT Retail gaining a competitive advantage over other altnets;

- setting in place a system that will help show greater transparency and allow for more effective exchange of information between BT and its wholesale customers;

- implementing an audit system managed by Ofcom or independent auditors to ensure good governance;

- forcing BT to comply with a set of KPIs and be financially liable in case of failure. Tele2, for example, quotes the example of Norway and argues that KPIs backed up by penalties could work better than any form of separation;

- ensuring that the access division receives actual payments (as opposed to transfer payments) from the rest of BT Group; and

- providing the right incentives and motivation for BT employees and management.

7.33 Because it submitted its response late, Energis was able to comment in its response on BT's organisational proposals. It believes that they will not deliver the expected results. Energis does not believe that an organisation with a public policy objective (i.e. the Access Services Division) can be run as part of a commercial organisation. It is also sceptical as to the rationale BT shareholders would have to invest in this organisation, and believes the formal role of the equality of access board is very unclear. Energis also highlights that BT's proposals only seem to deal with LLU and do not include PPCs, WLR and CPS. Energis has changed its position since Phase 1 (when it said that separation should be seen as a last resort) because it believes that BT is focused on equality of outcomes rather than inputs and, unlike other respondents, sees the practical issues around separation as surmountable.

7.34 Many respondents used other industries as benchmarks of successful implementation of separation or regulation of the natural monopoly. The gas industry was the most frequently quoted example.

Consumer and Citizen Issues

8.1   Ofcom believes that putting in place a platform for effective and sustainable competition in fixed telecoms going forwards is of critical importance for the businesses and consumers that buy telecoms services. However, the Phase 2 consultation also addressed two areas that affect citizens and consumers more directly. These were:

- searching and switching costs; and
- universal services

8.2   This section considers the responses to each of these issues in turn.

Search and Switching costs

Overview

8.3   This section covers all the issues raised by respondents in relation to consumer pricing information and awareness, cost and ease of switching suppliers. BT sees a case for Ofcom and intermediaries to provide information to consumers which encompasses more than just price, and it supports efforts by Ofcom to protect consumers against malpractices. Many altnets and service providers deny that there is a serious problem with consumers' access to information about the market, and many suggest that Ofcom leave it to the market and independent bodies to provide comparative information. Most altnets and service providers do, however, agree that there are issues around customer switching, highlighting in particular the lack of number portability for LLU and the lack of a fit-for-purpose WLR product. The cable companies argue that there is no need for Ofcom to regulate in this area. Mobile operators argue that in mobile, in particular, the market is delivering on this front and there is no need for further action by Ofcom. In contrast, consumer groups and some others have very serious concerns that competition alone cannot be relied upon to deliver accessible market information and easy switching to end users. Below we present the views from each category of respondent.

BT is supportive of the need for consumers to be well-informed and protected against mis-selling

8.4   BT uses Ofcom's research to demonstrate that the level of customer switching in fixed telephony services is reflective of the general consumer satisfaction with their provider and is not significantly lower than in the mobile market. BT also asserts that while both Ofcom and intermediaries could play a role in providing information to consumers, price is only part of the equation and other information on key indicators needs to be published. BT would welcome more guidance on comparative advertising, but it is against any restriction on tariff packages. On bill format, BT claims that it already dedicates significant resources to providing customer-friendly billing and that any standardisation effort will be extremely costly, except for the introduction of cross-industry terms and definitions. BT supports Ofcom's role in ensuring smooth switching processes and welcomes continued efforts by Ofcom to protect consumers against malpractices (mis-selling and slamming). Finally BT does not believe that it is the market's interest to encourage migration between tariffs offered by any one operator.

Altnets, service providers and alternative access infrastructure providers believe that Ofcom should act on supplier migration issues but leave pricing information to the market

8.5   The altnets, service providers and ISPs do not devote a lot of attention in their responses to consumer issues in general, and search and switching costs in particular. Most altnets support UKCTA's views, which in turn broadly endorse Ofcom's principles on provision of information, which include amongst others:

- encouraging markets to provide timely, objective, reliable information, with the possibility of regulatory intervention where appropriate (e.g. where Ofcom or Government has imposed a change on the market);

- ensuring communication is understood by all and that suppliers use the most appropriate communications channels to also take into account the interests of people with disabilities and those who do not speak English as a first language; and

- consulting relevant stakeholders as appropriate and reviewing information regularly to assess its impact.

8.6   With regards to intervention by Ofcom in providing more information to consumers, this group is generally in agreement that it is best to leave this to the market. Many providers, like Caudwell and France Telecom, believe that Ofcom should stand by its principles of minimum regulation in this area and should trust competition to deliver the outcomes that are in the best interests of customers. They argue that Ofcom should avoid erring on the side of over-regulation. Thus makes the specific point that it should not be assumed that pricing information should be provided on a strictly comparable basis, nor should there be a requirement for suppliers to converge towards more homogenous pricing plans. In the same vein, Carphone Warehouse believes that is unclear what further information would benefit consumers since telecoms offers have become easier for consumers to understand, especially with the development of "all-you-can-eat" offers. In contrast, IDT considers that comparability of pricing is a key issue and that is very difficult for consumers to understand the true price of a call.

8.7   Most of the respondents agree, though, that switching costs are a key issue and that Ofcom could do a lot to reduce them. Cable & Wireless argues that switching issues are linked to migration products. In particular C&W highlights the lack of number portability for LLU, the lack of access to BT's network access databases and the lack of fit-for-purpose WLR.

8.8   Most altnets believe that Ofcom has a role to play in ensuring customer switching is made easier. Tele2, in particular, argues that BT should be penalised if it can be proven that it is creating barriers to switching.

8.9   IDT provides a number of examples where it claims that BT creates barriers to switching. These include, for example, the fact that a customer wanting no longer to use BT, but instead to use another supplier for calls, has to request BT to change them to this option, giving BT the opportunity to engage in win-back tactics.

8.10   There is also broad consensus that Ofcom could do more to encourage customer switching not only by addressing migration costs but also by being more public in educating consumers on the benefits of switching.

8.11   France Telecom and Centrica are representative of many respondents in this group in believing that intermediaries can play a key role in consumer education and the

switching process. Centrica for example, is in favour of strengthening Ofcom's PASS accreditation scheme.

8.12 Some agree that there is scope to make billing easier to understand and that Ofcom could impose guidelines upon service providers.

Mobile players argue that the market is delivering in terms of providing clarity to customers on mobile supplier pricing

8.13 All of the mobile network operators use Ofcom's own research to argue that there is no problem to be addressed in mobile with respect to search and switching. They therefore support the "leave it to market option" with regards to Ofcom's role in regulating consumer information provision. France Telecom argues that competition rather than regulatory intervention is better able to ensure consumers are protected from excessive pricing and poor service. Vodafone acknowledges that some mobile tariffs can be found confusing; however it argues that each individual supplier tries to reduce complexity as part of its marketing and that a number of MVNOs position themselves on the basis of their simple tariff structures. It suggests that a well-functioning market provides satisfactory information for consumers' needs, not perfect information. It also points out that the greatest source of uncertainty is consumers' own expectations about their usage, and argues that the mobile sector has responded to this by offering packages and bundles.

Consumer groups argue for a better deal for end users

8.14 Consumer groups dedicate considerable effort to commenting on the issue of searching and switching. A number of them draw attention to Ofcom's research data as proof that many markets, and particularly the fixed call market, are not delivering the value of competition to consumers. For example, some point out that just 20% of consumers find it easy to compare prices for fixed calls, whereas 75% would use price comparisons. This group is unanimous in its view that there is a problem in provision of information to consumers (and businesses) to allow them to make informed choices. They typically believe that Ofcom's overall regulatory approach cannot deliver beneficial outcomes to consumers without the issue of search and switching being addressed through a more proactive approach by Ofcom.

8.15 *Access to information:* Many respondents sympathised with Ofcom's Advisory Committee for Older and Disabled People when it wrote that: *"quality and accessibility of information is vital to success in the telecoms market".* Many business and consumer groups argue for the more proactive engagement of Ofcom in information provision. On the business side, the Federation of small business (FSB) and Communications Management Association (CMA) think that it is hard for end users to judge value for money and ask Ofcom to be proactive in helping businesses make such comparisons.

8.16 Consumer groups generally think that leaving information needs to the market will not work, and urge Ofcom to be more proactive. The NCC points out that the reactive stance taken by regulators in the financial and energy markets were detrimental to consumer confidence and subsequently had to be reversed.

8.17 Many groups believe that although using intermediaries as a source of comparison is a good idea, the PASS scheme is not working well with only one web site so far accredited (uSwitch). Some respondents argue that Ofcom should provide information itself, like Energywatch; others are clear that Ofcom needs to address the issue, but

are less specific about the precise role that Ofcom should take. Ricability[3] points out that older and disabled people, in particular, need independent information to be able to benefit from competition. The Telecoms Ombudsman Service[4] suggests making it compulsory for service providers to publish common key data in the same way that U-Switch provides price comparisons. It also urges Ofcom to think about introducing a 'consumer charter'; a checklist of information which consumers can expect to be available from suppliers.

8.18 *Indicators of success:* Some respondents support the idea of Ofcom providing some key measures of success for defining effective competition which better address consumer needs, in particular availability of price information and fair distribution of the benefits of competition. The Ofcom Consumer Panel, for example, argues for the need of measurable indicators of success (of both consumer issues and overall approach) against which the regulatory record can be tracked.

8.19 With respect to *advertising*, many respondents, such as uSwitch, agree that Ofcom should encourage a responsible approach to service comparisons in advertising which would be beneficial in reducing the number of misleading comparisons.

8.20 Most respondents are wary about Ofcom *restricting the range of tariffs* that service providers are permitted to offer. Nonetheless, the NCC believes that the proposal is interesting, and suggests that Ofcom might define a range of standard products, without restricting the sale of others.

8.21 Regarding *billing*, there is a general agreement that further efforts are needed to make it easier for consumers to understand their bills. uSwitch argues that Ofcom could be working on this issue with associations such as the British Standards Institute in order to remove telecoms jargon that is not understood, or which could confuse consumers.

8.22 On *switching costs*, most organisations believe that it is inappropriate for Ofcom to ban retail switching costs but they welcome Ofcom's initiatives to minimise switching barriers. In particular, Ofcom could take a more proactive role and public position on switching by positively encouraging switching.

8.23 The Citizens Advice Bureau (CAB) listed a few switching malpractices where customers have been misled or refused their basic rights (for example, the 14 day right to return a mobile phone) and argue that it should be Ofcom's responsibility to stop such abuses.

8.24 Finally, opinions are mixed regarding any regulatory intervention on encouraging migration to cheaper tariff plans: for example NCC welcomes it, while uSwitch does not see the need to regulate.

Universal Service Obligation (USO)

Overview

8.25 Views on the need for a USO fund and how this should work vary widely. BT argues that its USO burden has become too high and states a clear preference for the establishment of a USO fund. Most altnets endorse the principle of a USO fund, but believe that this should only be implemented once there is clear evidence of equality of access and effective competition. Their view is that there is still a long way to go before the UK market arrives at this position. The mobile operators argue that the

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[3] Research Institute for Consumer Affairs
[4] Otelo

scope of universal services should not extend to mobile. Consumer groups express disappointment that the Telecoms Review does not place sufficient emphasis on universal services. They makes a number of detailed suggestions, including extending USO obligations to broadband and mobile, and ensuring that new telecoms products and services build functionality for disabled users in from the design phase.

BT suggests a move towards a consumer funded USO

8.26 BT welcomes the idea of a USO fund. It argues that its USO burden has become too high. Out of the options that Ofcom outlined, BT believes that consumer funding of the USO is the most transparent and realistic (followed by government funding). BT welcomes the idea of a bidding mechanism for delivery of USO.

Altnets and service providers believe it is too early to switch to a USO fund model

8.27 The majority of altnets and service providers agree that the concept of a USO fund could eventually become appropriate, but given the lack of competition and equality of access, argue that the UK telecoms market is still a long way from necessitating such a change. The only respondents from this group to express a different opinion were France Telecom and ISPA UK, who argue that the concept of a USO fund could be appropriate now. France Telecom in particular, states a preference for USO to be funded on the basis of either indirect levies on consumers or direct government funding.

8.28 Amongst the respondents who expressed a view, there is a general agreement that auctioning the delivery process of the USO should be considered once a fund is in place, and that USO should be technology-agnostic.

Mobile operators argue that USO should not apply to mobile

8.29 Many mobile operators did not express a view on USO. France Telecom, which includes Orange, agrees that USO should be technology-agnostic (i.e. the USO could be delivered via mobile) but argues that USO does not need to apply to mobile operators as prepay mobile telephony has already achieved the universal service objective in the mobile market.

Consumer Groups contest that the consultation does not focus enough on USO issues

8.30 The strong view of many consumer groups, especially those supporting the most vulnerable consumers, is that Ofcom's consultation did not adequately address universal service issues. At the centre of this, many associations don't understand why Ofcom is holding a separate review of the USO in parallel with the Strategic Telecoms Review. RNID, for example, raises a concern that USO issues could potentially end up falling through the gaps between the two consultations.

8.31 *Broadband USO:* a wide range of groups including Ricability, Ofcom's Advisory Committee for Older and Disabled people (ACOD), and business groups such as the CMA advocate the inclusion of broadband within the USO. FSB comments that it is especially concerned about the digital divide between the countryside and urban areas and suggests addressing this either through a broadband USO, or by allowing BT to continue cross-subsidising between urban and rural areas. The Telecoms Action Group (TAG) is disappointed that broadband is currently not part of the USO, particularly given the lead times involved in changing the USO. It points out that with the need to change the European Universal Services Directive, it might be years

before the issue can be considered again. The BSG make the point that whilst it is sympathetic to the view that not all individuals' basic needs may be met by the market, indications are that the market will deliver more than basic access to a very high percentage of the population within the near to medium term.

8.32 *Mobile and USO:* there are two issues at stake in the debate on mobile and USO. The first one deals with the delivery of USO over mobile. For many who expressed a view on this matter (e.g. TAG), the idea is appealing. However, according to the CAB, the availability of mobile services should not be a reason to dismantle the existing network of payphones as some consumers may be more comfortable with using legacy technology. The second issue is the support of USO funding by mobile operators. On this issue, there is a wide consensus among consumer groups (for example, represented by RNID and Ricability) that mobile companies should contribute to a future USO fund.

8.33 *Broadcasting and USO:* a few associations, including RNIB and Ofcom's Advisory Committee for Older and Disabled People (ACODP) point out that broadcasting obligations such as audio description and accessible programme guides need to be extended to cover broadcasting over telecoms networks.

8.34 *Building of USO requirements into new telecoms products from the start.* A number of consumer groups that represent the needs of particular types of vulnerable consumers insist that features for disabled customers need to be built into new products from the start. RNID emphasises that the cost of providing equality of access for disabled people can be trivial if built in at the design stage. A significant number of groups, including the Advisory Committee for Older and Disabled people and RNIB insist that requirements for disabled people be built into next generation networks from the start, and express concern that Ofcom has not been more vocal on the need for the inclusion of additional features at the design stage.

8.35 *Extending obligations to telecoms equipment manufacturers:* A few groups suggest that Ofcom should consider extending universal service obligations to telecoms equipment as well as to services. The Advisory Committee for Older and Disabled people quotes the example of the US where USO has already been extended to telecoms equipment.

8.36 *USO funding and delivery.* A wide consensus of consumer groups believes in the need for setting up a USO fund and that all providers should contribute, not just one provider as is the case at present. Some respondents in this group (for example, the RNID) support the concept of USO being contestable on the basis of who can deliver at "best value". A number of respondents argue that recipients of universal services should not be forced to receive them from a single supplier, but should have a choice of suppliers like other consumers.

Other respondents share many of the views of consumer groups

8.37 Many other respondents had similar views and concerns about USO as the consumer groups. However, a few additional points were made, some of which we mention below.

8.38 The Telecoms Association of the UK Water Industry (TAUWI) advocated that the USO should be funded in proportion to the profits of all service providers contributing to the fund.

8.39 A wide variety of proposals were made by individuals on the best way ways of delivering USO. While some propose a re-nationalisation of BT and the whole sector as the best way to go, Peter Weeks argues that now that mobile networks are cheap and widely available, the obligation to BT and Kingston on fixed networks should be removed. Tony Shipley mentioned some concerns on the USO funding with the gradual migration of traffic from traditional PSTN to VoIP, while Osney Consulting supported continuing with the status quo.

Section 9

Other

9.1 The Phase 2 consultation document addressed a wide range of issues relating to telecoms regulation, and the responses discussed an even wider range. Unfortunately, it is not possible to cover all these issues in this summary. However, we have covered a number of other issues in this section, which we have organised into the following categories:

- geographic regulation;

- broadband;

- next generation core networks;

- next generation access networks;

- cost of copper and cost of capital;

- mobile call termination;

- environmental issues; and

- wider value chain

Geographic regulation

BT is not opposed to Ofcom reflecting differences in competitive characteristics in different geographic areas

9.2 BT states that it is not opposed to a different set of regulations for different areas, based on the European Directive and as long as such obligations follow an SMP analysis per region. BT also suggests that Ofcom could consider a varying set of obligations if the competitive conditions in such areas vary.

9.3 Regarding the reporting of data on products on a geographical basis, BT says it is open to the idea but stresses that regular reporting should only be required where there is no competition (i.e. if an area is competitive now, the assumption should be that it will continue to be so).

Many service providers and altnets are strongly opposed to geographical differentiation

9.4 Most altnets and service providers do not support the concept of developing different sets of rules in different geographical areas, and strongly argue against it. UKCTA is representative of a number of them in articulating a concern for "unintended consequences", in particular "black holes" where BT's competitors are not able to supply. It argues that this would be especially damaging in the corporate market where there is a need for multi-site access. Other concerns expressed included:

- the practicality of collating information on a regional basis and the risk that the benefit may not outweigh the costs;

- the risk that Ofcom could be left powerless to act against margin squeeze in particular locations, which could allow BT to leverage market power from one geographic region to another;

- the danger that geographic de-averaging would exacerbate the digital divide, and that prices would be likely to increase in rural areas; and

- the potential for added consumer confusion if suppliers had to price on a regional basis.

9.5 UKCTA therefore calls for Ofcom to consult separately on the application of different regulation in different areas, before making any further moves in this direction.

9.6 A few respondents in this group are, however, more open to the idea of geographic differentiation of regulation. Centrica supports the idea of a regulated bitstream product where LLU is not commercially viable (for example, in rural areas). This idea is also supported by Tiscali. Video Networks Ltd (VNL) argues in favour of differing remedies at clusters of MDFs. Your Communications would be particularly supportive of initiatives from Ofcom to increase competition in suburban and rural areas, where it currently faces what it regards as "unfair" competition from BT, because of BT's de facto cross-subsidisation from urban areas. Your Communications argues that artificially low pricing by BT in less densely populated areas acts as a disincentive to other players to invest in alternative infrastructure.

9.7 Thus argues that if geographic variation of regulation was adopted, it should be in the form of carve-outs to national markets and changes to remedies rather than the definition of separate markets. Kingston invites Ofcom to undertake a local markets review and look to remove regulation where appropriate.

Alternative access infrastructure players have various views on the need for different regulation in different geographic areas

9.8 The views put forward by this group of respondents vary. NTL and UK Broadband believe that regulation based on a regional approach would be inappropriate. UK Broadband argues that this would be too intrusive, and could encourage cherry-picking by operators. Regarding the requirement to supply data on a regional basis, UK Broadband believes that this should only be the case where competition law issues arise. Telewest, however, is more open to the idea of varying regulation by geography, though it believes Ofcom should follow a "cautious and conservative" approach. It argues that in geographic areas where there is competition and contestability, Ofcom should rely on competition law only and BT should not be obliged to offer the same form of regulated products as elsewhere.

National and regional bodies are concerned about the prospects of a widening digital divide

9.9 Many national and regional groups believe that a digital divide is in prospect: between urban areas with a choice of leading-edge services; and less dense areas with no competition, and lower functionality and possibly more expensive services. Though they welcome regulation reflecting the differing competitive conditions in different areas, many are concerned that different regulation in different areas could widen this divide.

9.10 For example, the Northern Ireland DETI *"hopes that steps are taken such that digital divides do not emerge in the UK".* The Scottish Executive warns about the "glaring gap" between urban and rural areas as 8Mbit/s DSL services start being rolled out in most dense urban areas, leaving other parts of the country behind.

Broadband

9.11 BT and many other players agree that LLU is a viable solution in only 50% of the country. They argue that alternatives will therefore be required in other areas.

9.12 Many altnets argue that "naked DSL" (a wholesale product which excludes the costs specific to the PSTN, but included the costs of the copper loop) should be offered as soon as possible by BT. ISPA, for example, argues that naked DSL could be the way to remove economic bottlenecks to VoIP-type of services but that such a product should first be defined by the industry. Tele2 argues that naked DSL will be essential for competition in the market for triple play, will be crucial for making VoIP a success, and will be an effective tool for attacking BT's market power in retail line rental, which represents 30 to 50% of consumers' spend. A number of altnets warned Ofcom to be very cautious to ensure the appropriate allocation of costs between PSTN services and data services in such a wholesale product.

9.13 However, a number of altnets, and particularly those with LLU investments, are strongly opposed to the introduction of naked DSL. Easynet, for example, argues that it would need to be priced so as not to undermine LLU.

9.14 NTL and Telewest are in favour of naked DSL but argue that the cost of copper must be the same as in the line rental element of a narrowband line. UK Broadband takes a more sceptical stance on naked DSL, stating that it should not be assumed without further analysis that naked DSL requires regulation, and that naked DSL should be used only to provide broadband. In agreement with the cable operators, UK Broadband argues that BT should be allowed to cover its costs, including common costs previously covered by PSTN revenues.

Next Generation core Networks (NGNs)

BT will proceed with its 21CN investment if it receives explicit confirmation from Ofcom that it will be allowed to earn appropriate returns

9.15 BT argues that its NGN investment (called its 21st Century Network or 21CN) is currently the most advanced amongst European incumbent operators. However, BT states that it will only proceed with its 21CN deployment upon "Ofcom's explicit confirmation that we will be allowed to earn appropriate returns for a successful execution of 21CN".

9.16 BT then goes on to make a number of proposals to address some concerns and issues raised by Ofcom about access to the 21CN. In particular BT commits to the following:

- ensuring that there is an appropriate level of input from the industry into 21CN design by working with industry participants and Ofcom;

- reconsidering whether it will offer MSAN interconnect. BT says, however, that it doubts whether this is viable across all 5,500 MSANs;

- examining the commercial and technical feasibility of a viable method for ensuring that the "broadband dialtone" problem does not prejudice LLU operators;

- negotiating with industry on the issue of compensation for rearrangement of interconnection circuits as a result of the introduction of the 21CN. However, BT states that *"this must be balanced against the obsolete nature of some of the assets*

and the fact that industry players will participate in some of the 21CN savings as well as the benefits"; and

- implementing equivalence on 21CN systems and processes to appropriate SMP services through open interfaces.

Altnets and service providers voice concerns about BT's transparency on 21CN

9.17 Many altnets and service providers voice their strong concerns over the access arrangements to BT's 21CN. Many responses are not very detailed in this area, because Ofcom's separate consultation on the terms of access to next generation networks had only recently finished. However, many of this group see this issue as being key to sustainable and effective competition for many years to come.

9.18 UKCTA, Centrica and Your Communications and others argue for equivalence of input for 21CN products. Many, such as Centrica and Kingston, also argue that so far, BT's engagement with the rest of the industry has not been effective and that, generally speaking, BT has not been transparent enough about its plans for 21CN. These respondents stress how important it is that this issue is resolved quickly, or the window of opportunity to build pro-competitive access arrangements to the 21CN will be lost. They urge Ofcom to facilitate a dialogue between BT and other industry players to avoid upcoming disputes on standards, protocols and commercial principles. They also argue that they the need to know the details of BT's plans for 21CN, as these will guide their own investments.

9.19 Easynet voices it objections to MSAN interconnect, and emphasises the competitive threat from the 21CN's "broadband dialtone" capability. VNL also argues against MSAN interconnect and highlights its concern that this could undermine the LLU business model. Others, such as Tiscali, strongly support interconnection at the MSAN level.

9.20 Viatel argues that BT should offer a full range of access options to 21CN including naked DSL, MPLS with variable quality of service parameters and IP voice interconnect.

Manufacturers stress the importance of open standards and interoperability in the context of 21CN

9.21 A strong consensus of equipment manufacturers and technology companies strongly supports the creation of standards and interoperability from the design stage of the 21CN. For example, Nortel argues that these would need to include:

- access to a set of data interfaces, inter-module and signaling protocols, and APIs;
- the need to define the IP interface with control of quality of service;
- access to 'hooks' controlling quality of service, and other intelligence capabilities being as deep as the deepest API that does not compromise network security; and
- no proprietary standards once open ones have been agreed.

Consumer groups argue for the need to build in requirements for disabled groups at the design phase of 21CN products

9.22 Many consumer groups, associations and individuals did not comment on the quite technical issues around NGN access. However, some consumer groups protecting vulnerable consumers, such as the Advisory Committee for Older and Disabled People

expressed the need for product features geared towards disabled groups to be incorporated from the design phase.

Next Generation Access

9.23   In the Phase 2 consultation document, Ofcom proposed four options for the regulation of next generation access:

- equality of access to next generation access investments;

- equality of access, with returns adjusted to reflect the risk of making such investments;

- time-limited forbearance from regulation; and

- time-limited forbearance, subject to the investment being contestable by a variety of providers.

9.24   In addition, Ofcom discussed a number of structural options for the market.

BT argues for forbearance on next generation access

9.25   BT argues that since next generation access is an emerging market, there is no reason to assume that it will fail to be competitive. Therefore, BT favours forbearance, at least until it becomes clear that there is a situation of SMP. By refraining from regulating next generation access, Ofcom will create a climate promoting investment.

Altnets and service providers argue against forbearance but have divergent views on regulated returns

9.26   UKCTA believes that forbearance is not tenable. It argues that forbearance could only be appropriate where that the market is competitive enough or the investment is fully contestable. It does not believe that next generation access will not meet these criteria. Viatel, Carphone Warehouse, Cable & Wireless and the Association of Communications Service Providers amongst others put forward this argument and are opposed to forbearance. Carphone Warehouse argues that the principles of equivalence need to be applied to next generation access.

9.27   VNL argues that Ofcom should proceed with next generation access as it did with LLU, and only regulate it as a bottleneck if it is proven to be a bottleneck service. C&W argues that Ofcom should concentrate on getting LLU regulation in order, and that it is not clear today that there is any demand for next generation access, as copper could be enough to fulfil customers' needs for a long time. But some providers are prepared to contemplate a degree of forbearance. For instance, Thus thinks that forbearance could never be appropriate in residential markets, but could be possible in markets with high density of business customers.

9.28   Most altnets and service providers support the equality of access options put forward by Ofcom (Options A and B). UKCTA and Centrica support Option B, equality of access from outset with risk-adjusted rate of return, as they believe that investments in next generation networks will bear an additional amount of risk and future operators and investors should be rewarded appropriately. The counter argument from providers such as Viatel and Easynet, who support Option A, is that BT already has a stronghold in this market given its existing access infrastructure. This position of market power is unlikely to be broken. They are therefore in favour of Equality of Access with standard rates of return. C&W also concurs that at present, no expectation of higher regulated rate of return should be put in place.

9.29 For the most part, altnets and service providers think that next generation access will not be a contestable market. Viatel and Carphone Warehouse argue that given BT's position as owner of duct infrastructure, BT is likely to gain SMP in the next generation access market. Therefore, they believe that BT should be mandated to offer products such as dark fibre access.

9.30 Many altnets and service providers cautiously welcome Ofcom's discussions of various structural options, for example a structurally separate entity providing next generation local access, certain public sector ventures, use of alternative civil infrastructure etc. Many suggest that some of these structures could complement a policy of equality of access to next generation access infrastructure.

9.31 Thus and UKCTA both express particular concerns over any form of state aid or public sector subsidies for next generation access networks.

Alternative access infrastructure players highlight the potential of their networks to offer next generation access

9.32 NTL and Telewest both point out that the potential for next generation services to be provided over cable networks; they point out that BT will face competition in access. As a result, NTL argues for regulatory forbearance on any investment by BT. Telewest is in favour of ensuring that the investment opportunity is continuously contestable to players other than BT.

Other groups of respondents are divided on the appropriate regulation of next generation access

9.33 Not all other groups of respondents expressed a view on next generation access. Many emphasised how important the issue was for the UK. Marconi, for example, compared the roll-out of next generation access infrastructure with previous generations of infrastructure such as canals, railways and motorways. The CBI points out the role of such infrastructure in allowing UK businesses, and particularly small businesses, to benefit from sophisticated online transactional capabilities. The Fibre to the Home Council (FTTH Council) argued that next generation access is currently being provided at a sub-optimal rate, and that it is well within Ofcom's remit to investigate with the broadest scope what the barriers to this deployment could be. The Broadband Stakeholders' Group (BSG) agreed that the problem was fundamental, pointed out the potential for growth along the entire broadband value chain, and was concerned that regulatory intervention could deter investment or competitive entry. Both CWU and CMA believe that Ofcom and the UK telecoms industry should learn from the experience of other countries such as Japan which are already investing in FTTH. Peter Weeks believes that the focus for next generation access should be the upgrade of the local loop to fibre, while Osney Consulting argues that FTTH will be deployed sooner than expected.

9.34 A number of respondents urged Ofcom to think more broadly about next generation access than simply the four options that were posed. The Access to Broadband Campaign, for example, argued that the real competitive problem was in the middle mile, between peering point and exchange. Openhub and OpenPlanet pointed out the importance of a regulatory regime which allows community broadband schemes to interconnect to others' networks. Others, such as the FTTH Council, the BSG and Nortel, urged Ofcom to think laterally about some of the structural options that were discussed in the consultation document. The BSG made the point that the outcome of the Review should be to ensure that the financial return is high enough to secure next generation access investment and to provide incentive for market entry.

9.35 There was no clear consensus among other respondents on the four core options that Ofcom posed. For example some, like the CBI, argued for forbearance so long as the investment was made contestable. Others, such as OpenPlanet, strongly support Option B (equality of access with risk-adjusted returns); it thinks there is a strong risk of a monopolistic situation being re-created in next generation access.

Cost of copper and cost of capital

9.36 On these issues, most respondents commented that they will provide a more thorough analysis as part of their responses to Ofcom's parallel consultations.

BT argues that mandated rates of return should only apply to regulated activities

9.37 Ahead of its response to Ofcom's consultation on "Valuing the copper access", BT makes three specific points. Firstly, mandated returns should only apply to regulated activities and balance the effect on investment incentives and the protection of consumers from excessive charges. Secondly, the fact that assets are "already in the ground" should not be a determining consideration. Finally, aside from regulated activities, Ofcom should not be setting rates of return for BT.

Most altnets and service providers are in favour of rates of return that promote investment

9.38 The majority of altnets agree with UKCTA, ACSP and ISPA UK that different risk profiles of investment should justify different allowed rates of return, in order to promote investment. While dark fibre and copper access are all sunk costs with extremely low risk attached to them, downstream retail and wholesale services present higher risks and should therefore command a higher regulated cost of capital. However, a few service providers, including Centrica andViatel challenge the concept that 21CN and next generation access are risky investments. Viatel believes that the risks associated with BT's network are overstated. VNL argues that since revenues are predictable and interconnect arrangements will be likely to be favourable to BT, there is no justification for a higher rate of return.

9.39 Both Kingston and Thus also argue that Ofcom should not be influenced by a desire to lower the cost of WLR and LLU in reviewing the cost of copper. As Thus wrote: *"Provided that BT commits to delivering on equality of access, and subject to adequate margin squeeze safeguards, we would be happy with a regulatory settlement that rewards BT with a decent return on its copper infrastructure and next generation network investments".*

Mobile call termination

9.40 The Phase 2 document asked for suggestions as to other structures or regulatory options for mobile termination, which would allow Ofcom to adopt a less intrusive regulatory role than at present.

Mobile operators are in favour of deregulation of the mobile termination market

9.41 Many of the mobile operators argue that it is no longer appropriate for Ofcom to regulate mobile call termination at all. Vodafone, for example, argues that the disbenefits of unregulated termination are not proportionate to the intrusiveness of the regulation. O2 welcomes Ofcom's open approach to discussing different approaches to the call termination problem, and states that it intends to submit ideas on alternative termination structures.

Fixed operators, including BT and the altnets favour the current status quo on mobile termination

9.42 A number of fixed operators expressed an interest in alternative structures for call termination. However, most of them said that they found it difficult to think of other solutions that will succeed. BT argues that a "Receiving Party Pays" (RPP) structure could in theory render intrusive regulation of termination unnecessary. However, RPP will face a lot of practical hurdles (for example, cost of implementation and customer disruption). Regarding the impact of IP interconnection, UKCTA assesses that *"at present, we cannot see how the evolution to IP interconnection could introduce market mechanisms that would make such intrusive regulation unnecessary".* Fixed operators are therefore broadly unanimous on continuing with the status quo but are open to working with Ofcom to find a long term solution to the issue.

Environmental issues

9.43 Three respondents specifically focused on telecoms-related environmental issues. These include the Council of National Parks (CNP), Friends of the Lake District (FLD) and the Countryside Agency.

9.44 All of them raised the concern that the consultation did not place enough emphasis on environmental issues. CNP argues that the needs of National Parks (to conserve natural beauty and promote opportunities for the public to enjoy National Parks) have not been taken into account, and urges Ofcom to clarify in Phase 3 how it will take these into consideration. More specifically, FLD encourages Ofcom to recognise the issue of overhead telecommunication lines and their negative impact on the environment. It quotes the case of Ofgem, the electricity regulator, which has recently agreed to a £64 million expenditure plan in the next five years aimed at burying overhead wires and suggests that Ofcom considers a similar initiative.

Wider Value Chain

9.45 Ofcom also asked what its role should be in regulating the wider telecommunications value chain.

9.46 Many, such as the CBI, welcomed Ofcom looking at the issue in this breadth. However, the CBI argues that though Ofcom acknowledges these wider issues, it fails to consider them sufficiently centrally in its analysis of the telecoms sector.

9.47 The BSG states that Ofcom's role as regards the wider value chain should be to ensure that regulation does not undermine efficiency and investment. It argues that Ofcom should aim to minimise unintended consequences of regulation, and in particular, that a better understanding both of the economics of the content market and the specific demand for bandwidth from this market will facilitate this.

9.48 A number of responses raise specific issues in relation to the wider value chain. For example, British Music Rights emphasises how important copyright is to investment, and suggests that Ofcom works with Government to develop policy in this area. More generally, it argues that Ofcom should adopt a light-touch approach, based upon competition law and the promotion of interoperability.