

Wholesale unmetered narrowband Internet termination services - Hull area market

Identification and analysis of markets,
Determination of market power and
Setting of SMP conditions

Final Explanatory Statement and Notification

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Summary

A new regulatory regime

S.1 A new regulatory framework for electronic communications networks and services entered into force in the UK on 25 July 2003. The basis for the new framework is five new EU Communications Directives that are designed to create harmonised regulation across Europe.

S.2 The new Directives require National Regulatory Authorities ("NRAs"), amongst other things, to carry out reviews of competition in communications markets to ensure that regulation remains appropriate in the light of changing market conditions.

S.3 As part of this series of reviews, on 26 August 2003 Ofcom published a consultation document entitled *Wholesale unmetered narrowband Internet termination services - Hull area market* ("the August consultation document"). That document followed an earlier consultation document published on 17 March 2003 ("the March consultation document") and invited comments on the Director's proposal for defining the relevant wholesale market, assessment of competition and regulatory remedies in that market. The period of consultation closed on 26 September 2003.

S.4 As required by the Directives, the draft decision was also sent to the European Commission and to other NRAs as, in the Director's opinion, the proposal may have affected trade between Member States. The final decision included in this document is also being communicated to the European Commission.

Summary of decision

S.5 Having considered all responses to the August consultation document, the Director is setting out in the present document his final decision. This is summarised below.

Identification of markets

S.6 The wholesale services under consideration in this document are those such as HullPort24 which can be used by ISPs to provide retail unmetered narrowband Internet access. In relation to these wholesale services, the Director has decided to identify the following economic market in accordance with competition law principles, for the purpose of ensuring that regulatory obligations are proportionate and objectively justifiable;

- the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area.
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S.7 This market definition is unchanged from that proposed in the August consultation document.

Assessment of market power

S.8 The Director has decided that in the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area:

- Significant Market Power (SMP) held by Kingston Communications (Hull) plc ("Kingston")

S.9 This decision on SMP is unchanged from that proposed in the August consultation document.

Regulatory remedies

S.10 Given the position of dominance held by Kingston – ie: its ability to behave to an appreciable extent independently of competitors, customers and ultimately consumers, the Director has decided to impose conditions as follows in the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area:

- requirement to provide network access on reasonable request;
- requirement not to unduly discriminate;
- requirement to publish a reference offer;
- requirement to notify prices, terms and conditions; and
- requirement to notify technical information.

S.11 This decision on regulatory remedies is unchanged from that proposed in the August consultation document.

S.12 The new Directives allow Member States to carry forward some existing regulation until the market reviews have been completed and any new conditions put in place. As NRAs were not able to notify draft proposals to the European Commission before 25 July 2003, the Director issued notices to relevant communications providers to maintain some of the regulatory regime that existed before that date. For the market that is the subject of this document, specified licence conditions were made to continue in force by a notice given to Kingston on 23 July 2003 (the 'Continuation Notice'). This Continuation Notice came into effect on 25 July 2003.

S.13 As the Director has now decided to impose a number of conditions on Kingston in this market, the regulatory requirements that were continued beyond 25 July 2003 now need to be withdrawn. Those obligations include, among other things, requirements to supply to any person who reasonably requests such services in this market and not to show undue preference or discrimination in the provision of such services. This will require the Director to discontinue the

aforementioned provisions that were continued on 25 July. More details of the regulation to be removed, and how this will be done, are contained in Chapter 3 of this document.

Chapter 1

Background and consultation process

Scope of this review and the extent of existing regulation

1.1 This explanatory statement sets out the Director's conclusions with regard to the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area. This market includes wholesale services, for example HullPort24, which can be used by ISPs to provide retail unmetered narrowband Internet access services. Unmetered services provide dial-up Internet access on a flat rate basis with no call charges, as compared to metered services for which there are per minute call charges.

1.2 In relation to wholesale unmetered narrowband Internet termination services, Kingston is currently obliged to supply to any person who reasonably requests such services (Condition 43). Linked to this obligation is a prohibition on undue preference and undue discrimination (Condition 57) and the requirement for publication of charges, terms and conditions (Condition 58). Kingston currently provides services such as HullPort24 under these conditions.

The basis for market reviews

1.3 The review of competition completed by this document is a requirement of the new European regulatory framework for electronic communications networks and services, which entered into force on 25 July 2003. The framework is designed to create harmonised regulation across Europe and is aimed at reducing entry barriers and fostering prospects for effective competition to the benefit of consumers. The basis for the new regulatory framework is five new EU Communications Directives.

1.4 The new Directives require National Regulatory Authorities ("NRAs") such as Oftel to carry out reviews of competition in communications markets to ensure that regulation remains appropriate in the light of changing market conditions. This document concludes for this market the review process that the Director had commenced in anticipation of the new regime.

1.5 The detailed requirements and guidance concerning the conduct of market reviews are provided in the EU Communications Directives, the Act and in additional documents issued by the European Commission and Oftel. As required by the new regime, in conducting this review, Oftel has taken the utmost account of the Commission's *Recommendation on relevant product and service markets*, adopted on 11 February 2003 (the "Recommendation") and the Commission's guidelines on market analysis and the assessment of significant market power ("SMP") (the "SMP Guidelines").

1.6 Four of the new Directives were implemented in the UK on 25 July 2003. This was achieved via the Communications Act 2003 ("the Act"). The Act provides for functions, powers and duties to be carried by Ofcom, which include those flowing from those four EC Communications Directives. Certain existing functions are also transferred to Ofcom. However, Ofcom will not assume full functions under the Act until later this year. Accordingly, transitional arrangements are in place to enable the Director to carry out certain functions until they are transferred to Ofcom later in the year. Therefore, references in those provisions of the Act to Ofcom are, for the present time, to be read as references to the Director.

1.7 The August consultation document provides, in Chapter 1, more comprehensive details of:

- the purpose and objective of these new Directives;
- Oftel's powers to conduct market reviews; and
- the detailed procedural requirements and guidance that Oftel has taken into account in conducting this review, in order to define markets and to assess whether any providers have SMP.

Consultation processes

1.8 Oftel's consultation process for this market review began with a document published on 17 March 2003 ("the March consultation document"). That document invited comments on a proposal for a definition of the relevant market, an assessment of competition in the Hull area, and proposals for regulatory remedies on Kingston. That consultation closed on 30 May 2003.

1.9 A second stage of consultation began on 26 August 2003. The August consultation document updated the analysis, based on market developments and responses to the first stage of consultation. The second stage of consultation, which closed on 26 September 2003, invited representations from UK stakeholders, the European Commission and other NRAs.

1.10 NRAs must send the European Commission a summary notification form of their draft proposals. Oftel's notifications are published on the European Commission's website at <http://forum.europa.eu.int/Public/irc/infso/ecctf/library?l=/uk&vm=detailed&sb=Title>

Summary of the latest consultation

1.11 This statement should be read in conjunction with Oftel's March and August consultation documents to understand the full reasoning for the Director's decision.

1.12 The August consultation document laid out the Director's proposed market definition, the proposal that Kingston should be designated with SMP and the

regulatory remedies to be imposed. A summary of responses is contained in Annex B.

1.13 The Director has considered the responses carefully and taken utmost account of the points made when setting out in the present document his final decision on market definition, the making of market power determinations and the setting of SMP conditions. Where new and substantive points are made, they are addressed in Chapter 2 below. Where points were repeated from the first stage of consultation, and have thus been considered already in Oftel's analysis, this document does not reprise Oftel's previous response.

1.14 The Director's formal Notification of this decision, as required under section 48(1) and section 79 of the Act, is provided at Annex A.

Chapter 2

Final decision

2.1 The Director's final decision, taking full account of representations from all stakeholders is set out below, covering:

- market definition;
- an assessment of whether any network operators have SMP; and
- the regulatory remedies.

2.2 Section 79(1) of the Act provides that before a market power determination may be made, the Director must (i) identify the markets which are, in his opinion, the ones which, in the circumstances of the UK, are the markets in relation to which it is appropriate to consider such a determination; and (ii) analyse those markets. The Director is, as noted above, required to take due account of all applicable guidelines and recommendations issued by the European Commission. Under section 79(4) of the Act, the Director may identify markets and make market power determinations by way of publication of a notification. The notification at Annex A is such a notification.

Market definition

2.3 The Director has decided to define the relevant economic market as:

- the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area.

2.4 The chief features of the market definition remain as proposed in the August consultation document (at Chapter 2 and Annexes A and B).

2.5 In response to the August consultation document, stakeholders generally agreed or had no comment on the relevant economic market for this review (see Annex B). Where comments were received, these focussed on the approach and methodology Oftel had used rather than conclusions that Oftel had reach with regard to the relevant market.

2.6 The comments that were received from the European Commission and one other respondent focus on aspects of Oftel's methodology for the analysis of demand-side substitutes at the retail level and the approach to wholesale market definition. Oftel has responded in detail to the points raised in relation to the market definition in Annex C.

Retail level demand-side substitution

2.6 In relation to Oftel's demand side analysis at the retail level, one respondent comments on Oftel's SSNIP (small but significant, non-transitory price increase) test, in particular the critical loss factor and interpretation of consumers reactions to a 10% price increase. However even taking into account some of the revised assumptions that the respondent suggests, Oftel's view is that the revised critical loss estimates are still consistent with Oftel's conclusions at the retail level. In particular Oftel would stress that:

- Oftel's analysis does not rest solely on the stated switching percentages. They are used to complement consumer survey information on usage patterns and reasons for use of particular packages.
- The calculation is relatively conservative because Oftel's previous market research has found that fewer customers actually switch than claim they would in response to a hypothetical question about switching behaviour. Therefore the survey results are expected to be over-estimates of switching behaviour.

Wholesale market definition

2.7 The European Commission and one other respondent comment that Oftel's demand side analysis at the wholesale level could take into account demand in addition to the derived demand from unmetered retail services. The European Commission notes that unmetered wholesale services could be used for retail services other than just unmetered Internet access.

2.8 Oftel accepts that unmetered wholesale services can in principle be used for a number of retail services, although is not aware that this is currently widespread in the UK. However, the affect of this on demand conditions at the wholesale level would still be considered in the context of looking at demand derived from the retail level. In fact Oftel effectively considered the extent of wholesale demand-side substitutability at the wholesale level by assessing the nature of supply-side substitutability at the retail level. Therefore, Oftel's derived demand approach is consistent with the observations made by the European Commission and the other respondent.

SMP assessment

2.9 As referred to above, under section 79(1) of the Act the Director must carry out an analysis of identified markets before making a market power determination. Further, section 45 of the Act details the various conditions that may be set under the new regulatory regime. Section 46 details upon whom those conditions may be imposed. In relation to SMP services conditions, section 46(7) provides that they may be imposed on a particular person who is a communications provider or a person who makes associated facilities available and who has been determined to have SMP in a "services market" (ie: a specific market for electronic communications networks, electronic communications services or associated facilities). Accordingly, having identified the relevant markets as above, the Director is required to analyse those market in order to assess whether any person

or persons have SMP as defined in section 78 of the Act (which implements Article 14 of the Framework Directive).

2.10 The Director has decided that, in the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area:

- Significant Market Power (SMP) held by Kingston Communications (Hull) plc ("Kingston").

2.11 This assessment on SMP is unchanged from the August consultation document, which contained comprehensive details of Oftel's analysis (at Chapter 3). Oftel has reviewed that analysis in the light of representations made by stakeholders.

2.12 In response to the August consultation document, Kingston re-iterates their comment made in response to the March consultation that the Internet access market in the Hull area is fully contestable on an end-to-end basis.

2.13 In the August consultation document Oftel noted that in a contestable market potential entrants face no barriers to entry, in particular there must be no sunk costs at all, and that there be significant sunk costs for entry in the Hull area using alternative technologies. In response Kingston has asserted that it is quite possible to develop a market entry strategy based on radio access systems that does not lead to significant sunk costs at all.

2.14 Oftel does not agree that entering the Hull area using radio access systems would not lead to significant sunk costs. In particular, there would at least be sunk costs associated with the building of base station sites, the installation of equipment and the provisioning of leased lines. In addition, the competitive impact of such services is currently unproven and Oftel considers that they are unlikely to have a significant effect during the time scale of the market review. As such, the tests for contestability are not met for wholesale services in the Hull area.

Regulatory remedies

2.15 The formal statement of the Director's decision on market definition and SMP is made by means of a Notification under section 48(1) and section 79 of the Act. This Notification is at Annex A below.

2.16 As discussed in paragraphs 4.9 to 4.10 of the August consultation document, and in light of his duties in Section 4 of the Act, the Director's view is that the aim of the regulatory remedies should be to promote competition in relation to the provision of retail unmetered narrowband Internet access services in the Hull area.

2.17 Given the position of dominance held by Kingston – ie: its ability to behave to an appreciable extent independently of competitors, customers and ultimately consumers, and having considered the responses to the August consultation, the

Director has decided to impose conditions as follows in the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area:

- requirement to provide network access on reasonable request;
- requirement not to unduly discriminate;
- requirement to publish a reference offer;
- requirement to notify prices, terms and conditions; and
- requirement to notify technical information.

2.18 This decision on regulatory remedies is unchanged from that proposed in the August consultation document.

2.19 In response to the August consultation document, Kingston comments that in the absence of any evidence that the services currently offered by Kingston are unreasonable, no further ex ante regulation is required.

2.20 Of tel does not consider that evidence on the unreasonableness of services currently provided under the pre-July 2003 regulatory framework is relevant to the consideration of appropriate regulatory remedies under the new regulatory framework. In particular, the decision to impose a network access condition does not make any judgements about the reasonableness of current products, its purpose is to ensure that third parties, ie ISPs, are able to make reasonable requests for wholesale services in the future. In the absence of such a condition Kingston would in the future be able to deny access, or offer it on unreasonable terms so as to prevent entry and competition developing at the retail level.

2.21 The conditions relating to the Director's decision are Condition A1, Condition A2, Condition A3, Condition A4 and Condition A5 as set out in Annex E. The tests under the Act set out in the March and August consultation documents are relevant and are summarised below.

Requirement to provide network access on reasonable request - SMP condition A1

2.22 In the Director's view, this condition meets the tests set out in Section 47 of the Act, being objectively justifiable, non discriminatory, proportionate and transparent.

2.23 The Director considers that the network access condition is objectively justifiable as it would allow ISPs to provide retail unmetered narrowband Internet access services and compete with Kingston's own ISP, Karoo, therefore promoting competition in the retail market. In the absence of such a requirement Kingston may refuse reasonable requests for access or provide access on unreasonable terms. Provision of unmetered Internet access services would then be limited because potential competitors would not have access to appropriate wholesale inputs. The difference in treatment of BT and Kingston is not discriminatory

because the Director's decision is that Kingston has SMP in the market whereas BT does not. The condition is proportionate, since it does not require Kingston to provide access if a request for access is not reasonable. The Director has set out how he might assess whether demands for access are reasonable in the Access Guidelines referred to above and therefore the obligation meets the requirement of transparency set out in the Act.

2.24 In addition, the Director has taken into account the factors set out in section 87(4) of the Act and in particular the need to ensure that requests for access are reasonable and technically feasible as set out in the Access Guidelines (http://www.oftel.gov.uk/publications/ind_guidelines/acce0902.htm)

Requirement not to unduly discriminate - SMP condition A2

2.25 In the Director's view, this condition meets the tests set out in Section 47 of the Act, being objectively justifiable, non discriminatory, proportionate and transparent.

2.26 The Director considers that the condition is objectively justifiable, in that it provides safeguards to ensure that competitors, and hence consumers, are not disadvantaged by Kingston discriminating in favour of its own ISP. It is proportionate in that discrimination is only prohibited if it is undue. The difference in treatment of BT and Kingston is not discriminatory because the Director's decision is that Kingston has SMP in the market whereas BT does not. It is transparent because the condition that would apply to Kingston is clearly set out in this document.

Requirement to publish a reference offer – SMP condition A3

2.27 In the Director's view, this condition meets the tests set out in Section 47 of the Act, being objectively justifiable, non discriminatory, proportionate and transparent.

2.28 The Director considers that the condition to publish a reference offer is objectively justifiable in so far as it provides information to prospective market entrants in order to encourage competition in markets where SMP is persistent. It assists transparency for the monitoring of potential anti-competitive behaviour and to give visibility to the terms and conditions on which other providers will purchase wholesale access services. This helps to ensure stability in markets and without it, incentives to invest might be undermined and market entry made less likely. Without such a published offer, market entry might be deterred to the detriment of the long term development of competition and hence consumers.

2.29 It is proportionate, in that it does not impose regulation beyond that required to encourage competition. The difference in treatment of BT and Kingston is not discriminatory because the Director's decision is that Kingston has SMP in the

market whereas BT does not. It is transparent because the condition that would apply to Kingston is clearly set out in this document.

Requirement to notify charges terms and conditions - SMP condition A4

2.30 In the Director's view, this condition meets the tests set out in Section 47 of the Act, being objectively justifiable, non discriminatory, proportionate and transparent.

2.31 The Director considers that the condition is objectively justifiable, in that the benefits of price publication and notification outweigh the disadvantages. It is proportionate, as it does not require publication of any details that would not be available in a normal commercial contract. The Director's view is that a notification period of 90 days is appropriate where SMP is considered persistent. The difference in treatment of BT and Kingston is not discriminatory because the Director's decision is that Kingston has SMP in the market whereas BT does not. It is transparent because the condition that would apply to Kingston is clearly set out in this document.

Requirement to notify technical information – SMP condition A5

2.32 In the Director's view, this condition meets the tests set out in Section 47 of the Act, being objectively justifiable, non discriminatory, proportionate and transparent.

2.33 The Director considers that the condition is objectively justifiable as it enables competing operators to make full and effective use of Network Access covered by Condition A1. The difference in treatment of BT and Kingston is not discriminatory because the Director's decision is that Kingston has SMP in the market whereas BT does not. It is proportionate, since 90 days is the minimum necessary to allow effective use to be made of Network Access; and it is transparent because the condition that would apply to Kingston are clearly set out in this document.

Future reviews

2.34 Of tel considers it important to continue to monitor this market. However, Of tel is not able to comment on the possible requirement and timing for any future review as this will be a matter for Of com to decide.

Chapter 3

Discontinuation of current regulation

Introduction

3.1 The new Directives allow Member States to carry forward some existing regulation until the market reviews have been completed. The power for the Director to do this is contained in paragraphs 9 and 22 of Schedule 18 to the Communications Act 2003 (the 'Act'). As national regulatory authorities ('NRAs') were not able to notify draft proposals to the European Commission before 25 July 2003, the Director issued continuation notices to relevant communications providers to maintain some of the regulatory regime that existed before that date.

3.2 For the market that is the subject of this document, specified licence conditions were made to continue in force by a continuation notice given to Kingston on 23 July 2003 (the 'Continuation Notice'). That Continuation Notice came into effect on 25 July 2003. Further details are contained in the Director's consultation document (www.oftel.gov.uk/publications/licensing/2003/cont0703.htm) and statement (www.oftel.gov.uk/publications/eu_directives/cont_notices/cont0903.pdf) on the continuation process.

3.3 Paragraph 9 (11) of Schedule 18 to the Act imposes a duty on the Director, as soon as reasonably practicable after giving such a Continuation Notice, to take the necessary steps to enable him to decide whether or not to set a condition (including a SMP condition) for the purpose of replacing the continued obligation. When he has done so, paragraph 9 (12) of Schedule 18 to the Act requires the Director to give a notice that the continuation notice ceases to have effect, and that he must do this as soon as reasonably practicable after taking a decision to impose (or not to impose) conditions under the new regime.

3.4 As mentioned in paragraph 1.2 of the August consultation document, the regulation applying to Kingston in the unmetered narrowband Internet termination market is the obligation to supply to any person who reasonably requests such services (Condition 43). Linked to this obligation is a prohibition on undue preference and undue discrimination (Condition 57) and the requirement for publication of charges, terms and conditions (Condition 58).

3.5 As the Director has concluded that the SMP conditions set out in Chapter 2 of this explanatory statement should apply in the market covered in this review, the present regulatory requirements on Kingston set out in its Continuation Notice in respect of the market defined in this document will now be discontinued. This will require the Director to give a notice (the 'Notice') to discontinue the relevant provisions that were continued on 25 July. The discontinuation Notice for Kingston is included at Annex D of this explanatory statement.

The effect of the discontinuation Notice will be to discontinue the continued condition 43; in so far as it applies to the market identified in this document.

The process for discontinuing continued provisions in Continuation Notices

3.6 The Director recently issued a consultation document “Discontinuing licence conditions after 25th July 2003” of 2 October 2003 (available at http://www.oftel.gov.uk/publications/eu_directives/2003/discont1003.pdf) (the “October consultation document”), which consulted on the model discontinuation notice, the process for discontinuation and the appropriateness of discontinuing particular obligations including in respect of this particular market review.

3.7 At paragraph 13 of the October consultation document, the Director explained that Condition 43, which is a continued provision contained in Schedule 1 of Kingston's Continuation Notice, has been continued in respect of Kingston. He stated that Condition 43 will be discontinued on a market by market basis. He also stated that where appropriate he will provide an indicative opinion on the services included in Condition 43 which are to be discontinued for the purposes of a particular market review (see below).

3.8 In so far as Conditions 57 and 58 are concerned, the Director set out at paragraph 11 of the October consultation document his view that that obligation only applies where certain obligations are in place, for example Condition 43. He therefore did not consider it necessary to discontinue Conditions 57 and 58 on a market-by-market basis since they will cease to apply when other obligations, such as Condition 43, are discontinued, which will be on market by market basis. He proposed that Conditions 57 and 58 are discontinued formally once the whole market review process has been completed. The Director received no responses to the October consultation document which led him to change that view.

3.9 Some continued provisions in Kingston's Continuation Notice relate to other market reviews. As market reviews are likely to be completed at different times, this raises an issue about when to give notice that a Continuation Notice ceases to have effect. Therefore, the Director has decided to discontinue continued licence conditions for the purposes of a particular market at the time when that market review is completed and any new obligations in that market are imposed. The other licence conditions in Kingston's Continuation Notice will, however, continue to have effect through the Continuation Notice in relation to other markets where the relevant review has not been completed because the notice would only have ceased the Continuation Notices in part.

3.10 As stated in paragraph 3 of the Statement “Discontinuing Licence Conditions” published on 13 November 2003, the Director received three responses to that consultation, but none of the points raised were specific to the process of discontinuation of regulations relating to this market. The regulations to be discontinued in this market therefore remain as set out in the Discontinuation statement.

The Discontinuation Notice

3.11 The Notice given under paragraph 9 (9) of Schedule 18 to the Act to discontinue Condition 43 is included at Annex D to this explanatory statement. The effect of that discontinuation Notice will be to discontinue the continued Condition 43, in so far as it applies to the market covered by this review.

3.12 The following is a non-exhaustive, indicative list of those services which the Director considers that Condition 43 will be discontinued in respect of, to the extent that they relate to this market review:

Kingston Products

- **Wholesale Unmetered narrowband Internet termination**
HullPort24
- **Products which are included, in part, in the unmetered narrowband Internet termination market**
Connect Narrowband

The Notice is deemed to be effected a day after publication and posting of the Notice. This is because paragraph 9 (12) (b) of Schedule 18 to the Act states that where the Director has decided to set a condition, a Notice under paragraph 9 (9) of Schedule 18 to the Act cannot be given until that condition is in force. Therefore, the discontinuation Notice cannot be given until the new SMP conditions are made. In addition, in accordance with section 7 of the Interpretation Act 1978 and section 394 (7) of the Communications Act 2003, as the discontinuation Notice is being served by post, it will be deemed to be effected a working day after posting, which is 1 December 2003.

Annex A

Notification of the identification of certain services markets, the making of market power determinations and the setting of SMP services conditions

NOTIFICATION PURSUANT TO SECTIONS 48(1) AND 79 OF THE COMMUNICATIONS ACT 2003

The identification of certain services markets, the making of market power determinations in relation to those markets and the setting of SMP services conditions under section 45 of the Communications Act 2003

WHEREAS:

- (i) the Director General of Telecommunications (the “Director”), in accordance with Regulation 6 of the Electronic Communications (Market Analysis) Regulations 2003, made a proposal for identifying a market and making a market power determination in relation to that market and the setting of SMP services conditions in relation to Kingston by publication of a notification on 14 March 2003 ('the First Notification');
 - (ii) however, in April 2003, the European Commission advised national regulatory authorities that such a notification could not be made under Article 7 of the Framework Directive (Directive 2002/21/EC) before 25 July 2003. In addition, the Electronic Communications (Market Analysis) Regulations 2003 were replaced by the Communications Act 2003 (the “Act”) on that date;
 - (iii) by virtue of the Communications Act 2003 (Commencement No. 1) Order 2003 (S.I. 2003/1900 (C.77)) made under sections 411 and 408 of the Act:
 - a) certain provisions of the Act were commenced on 25 July 2003 for the purpose only of enabling the networks and services functions under those provisions to be carried out by the Director; and
 - b) those provisions of the Act are to have effect as if references to Ofcom were references to the Director;
 - (iv) consequently, in accordance with sections 48(2) and 80 of the Act, the Director issued a further notification setting out his proposals for the identification of services markets, the making of market power determinations in relation to those markets and the setting of SMP services
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conditions in relation to Kingston on 26 August 2003 (the 'Second Notification');

- (v) the Director invited representations about any of the proposals set out in the First and Second Notifications and the explanatory statement accompanying the First and Second Notifications by 30 May 2003 and 26 September 2003 respectively;
 - (vi) a copy of the Second Notification was sent to the Secretary of State in accordance with section 50(1)(a) of the Act, and to the European Commission and to the regulatory authorities of every other member State in accordance with sections 50(3) and 81 of the Act;
 - (vii) by virtue of section 80(6) of the Act, the Director may give effect to any proposals to identify a market for the purposes of making a market power determination or any proposals for making a market power determination set out in the Second Notification, with or without modifications, where:
 - a) he has considered every representation about his proposals made to him within the period specified in the Second Notification;
 - b) he has had regard to every international obligation of the United Kingdom (if any) which has been notified to him for this purpose by the Secretary of State; but,
 - c) the Director's power to give effect to such proposals is subject to section 82 and 83 of the Act;
 - (viii) by virtue of section 48(5) of the Act, the Director may give effect to any proposals to set SMP services conditions set out in the Second Notification, with or without modification, where:
 - (a) he has considered every representation about the proposals made to him within the period specified in the Second Notification; and
 - (b) he has had regard to every international obligation of the United Kingdom (if any) which has been notified to him for this purpose by the Secretary of State;
 - (ix) the Director has considered every such representation made to him in respect of the proposals set out in the First and Second Notifications and the accompanying explanatory statements; and the Secretary of State has not notified the Director of any international obligation of the United Kingdom for this purpose;
 - (x) the European Commission has not made a notification for the purposes of Article 7(4) of the Framework Directive as referred to in section 82 of the Act and the proposal does not relate to a transnational market as referred to in section 83 of the Act;
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THEREFORE

1. The Director General of Telecommunications ('the Director') in accordance with section 79 of the Act:

(a) identifies the following market for the purpose of making a market power determination:

the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area; and

b) makes the following market power determination that the following person has significant market power:

in relation to the market referred to in paragraph 1 (a) above, Kingston.

2. In accordance with sections 48(1) and 79 of the Act, the Director hereby sets pursuant to section 45 of the Act the SMP services conditions on the person referred to in paragraph 1 (b) above as set out in the Annex to this notification (this 'Notification') to take effect, unless otherwise is stated in the Annex to this Notification, on the date of publication of this Notification.
 3. The effect of, and the Director's reasons for identifying the market set out in paragraph 1 (a) above, is contained in Chapter 2 of the explanatory statement with this Notification and Chapter 2 and Annexes A and B of the explanatory statement accompanying the Second Notification.
 4. The effect of, and the Director's reasons for making the market power determination in paragraph 1(b) above, is contained in Chapter 2 of the explanatory statement with this Notification and Chapter 3 of the explanatory statement accompanying the Second Notification.
 5. The effect of, and the Director's reasons for the setting of, the SMP services conditions set out in the Annex to this Notification are contained in Chapter 2 of the explanatory statement accompanying this Notification and Chapter 4 of the explanatory statement accompanying the Second Notification.
 6. In making the decisions referred to in paragraph 1 above, the Director has taken due account of all applicable guidelines and recommendations which have been issued or made by the European Commission in pursuance of a Community instrument, and relate to market identification or analysis, as required by section 79 of the Act.
 7. In making the decisions referred to in paragraphs 1 and 2 above, the Director has considered and acted in accordance with the six Community requirements set out in section 4 of the Act.
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8. The Director considers that the SMP services conditions referred to in paragraph 2 above comply with the requirements of sections 45 to 47, and 87 of the Act, as appropriate and relevant to each such SMP condition.
9. The Director has sent a copy of this Notification to the Secretary of State in accordance with sections 50(1)(a) and 81(1) of the Act and to the European Commission in accordance with sections 50(2) and 81(2) of the Act.
10. Save for the purposes of paragraph 1 (a) of this Notification and except as otherwise defined in this Notification, words or expressions used shall have the same meaning as in the Act.
11. In this Notification:
 - (a) **"Hull area"** means the area defined as the 'Licensed Area' in the licence granted on 30 November 1987 by the Secretary of State under section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc.
 - (b) **"Kingston"** means Kingston Communications (Hull) plc, whose registered company number is 2150618, and any of its subsidiaries or holding companies, or any subsidiary of such holding companies, all as defined by Section 736 of the Companies Act 1985 as amended by the Companies Act 1989.

DAVID ALBERT EDMONDS

DIRECTOR GENERAL OF TELECOMMUNICATIONS

27 November 2003

Annex

The conditions imposed on Kingston under sections 45 and 87 of the Communications Act 2003 as a result of the analysis of the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area in which Kingston has been found to have significant market power

Part 1: Definitions and Interpretation of these conditions

1. These conditions shall apply to the market for wholesale unmetered narrowband Internet termination for Internet traffic originating in the Hull area.
 2. For the purpose of interpreting the conditions imposed on the Dominant Provider following a review of the market referred to in paragraph 1 of this Notification the following definitions shall apply:

“Act” means the Communications Act 2003;

“Access Charge Change Notice” has the meaning given to it in Condition C 4.2;

“Director” means the Director General of Telecommunications as appointed under section 1 of the Telecommunications Act 1984;

“Dominant Provider” means Kingston Communications (Hull) plc ('Kingston'), whose registered company number is 2150618, and any of its subsidiaries or holding companies, or any subsidiary of such holding companies, all as defined by Section 736 of the Companies Act 1985 as amended by the Companies Act 1989;

“Reference Offer” means the terms and conditions on which the Dominant Provider is willing to enter into an Access Contract;

“Third Party” means either a person providing a Public Electronic Communications Service or a person providing a Public Electronic Communications Network.
 3. Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them in paragraph 2 of this Part above and otherwise any word or expression shall have the same meaning as it has in the Act.
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4. The Interpretation Act 1978 shall apply as if each of the conditions were an Act of Parliament.
5. Headings and titles shall be disregarded.

Part 2: The conditions

Condition C1 – Requirement to provide network access on reasonable request

C1.1 Where a Third Party reasonably requests in writing Network Access, the Dominant Provider shall provide that Network Access. The Dominant Provider shall also provide such Network Access as the Director may from time to time direct.

C1.2 The provision of Network Access in accordance with paragraph C1.1 shall occur as soon as reasonably practicable and shall be provided on fair and reasonable terms, conditions and charges and on such terms, conditions and charges as the Director may from time to time direct.

C1.3 The Dominant Provider shall comply with any direction the Director may make from time to time under this Condition.

Condition C2 – Requirement not to unduly discriminate

C2.1 The Dominant Provider shall not unduly discriminate against particular persons or against a particular description of persons, in relation to matters connected with Network Access.

C2.2 In this Condition, the Dominant Provider may be deemed to have shown undue discrimination if it unfairly favours to a material extent an activity carried on by it so as to place at a competitive disadvantage persons competing with the Dominant Provider.

Condition C3 – Requirement to publish a reference offer

C3.1 Except in so far as the Director may otherwise consent in writing, the Dominant Provider shall publish a Reference Offer and act in the manner set out below.

C3.2 Subject to paragraph C3.8 below, the Dominant Provider shall ensure that a Reference Offer in relation to the provision of Network Access includes at least the following:

- (a) a description of the Network Access to be provided, including technical characteristics (which shall include information on network configuration where necessary to make effective use of the Network Access);
 - (b) the locations of the points of Network Access;
 - (c) the technical standards for Network Access (including any usage restrictions and other security issues);
 - (d) the conditions for access to ancillary, supplementary and advanced services (including operational support systems, information systems or databases for pre-ordering, provisioning, ordering, maintenance and repair requests and billing);
 - (e) any ordering and provisioning procedures;
 - (f) relevant charges, terms of payment and billing procedures;
 - (g) details of interoperability tests;
 - (h) details of traffic and network management;
-

(i) details of maintenance and quality as follows:

- (i) specific time scales for the acceptance or refusal of a request for supply and for completion, testing and hand-over or delivery of services and facilities, for provision of support services (such as fault handling and repair);
- (ii) service level commitments, namely the quality standards that each party must meet when performing its contractual obligations;
- (iii) the amount of compensation payable by one party to another for failure to perform contractual commitments;
- (iv) a definition and limitation of liability and indemnity; and
- (v) procedures in the event of alterations being proposed to the service offerings, for example, launch of new services, changes to existing services or change to prices;

(j) details of measures to ensure compliance with requirements for network integrity;

(k) details of any relevant intellectual property rights;

(l) a dispute resolution procedure to be used between the parties;

(m) details of duration and renegotiation of agreements;

(n) provisions regarding confidentiality of non-public parts of the agreements;

(o) rules of allocation between the parties when supply is limited (for example, for the purpose of co-location or location of masts);

(p) the standard terms and conditions for the provision of Network Access.

C3.3 To the extent that the Dominant Provider provides to itself Network Access that:

(i) is the same, similar or equivalent to that provided to any Third Party; or

(ii) may be used for a purpose that is the same, similar or equivalent to that provided to any Third Party,

in a manner that differs from that detailed in a Reference Offer in relation to Network Access provided to any Third Party, the Dominant Provider shall ensure that it publishes a Reference Offer in relation to the Network Access that it provides to itself which includes, where relevant, at least those matters detailed in Condition C3.2(a)-(p).

C3.4 The Dominant Provider shall, within one month of the date that this Condition enters into force, publish a Reference Offer in relation to any Network Access that it is providing as at the date this Condition enters into force.

C3.5 The Dominant Provider shall update and publish the Reference Offer in relation to any amendments or in relation to any further Network Access provided after the date this Condition enters into force.

C3.6 Publication referred to above shall be effected by:

(a) placing a copy of the Reference Offer on any relevant website operated or controlled by the Dominant Provider; and

(b) sending a copy of the Reference Offer to the Director.

C3.7 The Dominant Provider shall send a copy of the current version of the Reference Offer to any person at that person's written request (or such parts which have been requested).

C3.8 The Dominant Provider shall make such modifications to the Reference Offer as the Director may direct from time to time.

C3.9 The Dominant Provider shall provide Network Access at the charges, terms and conditions in the relevant Reference Offer and shall not depart therefrom either directly or indirectly.

C3.10 The Dominant Provider shall comply with any direction the Director may make from time to time under this Condition.

Condition C4 – Requirement to notify charges and terms and conditions

C4.1 Except in so far as the Director may otherwise consent in writing, the Dominant Provider shall publish charges, terms and conditions and act in the manner set out below.

C4.2 Save where otherwise provided in Condition C5, the Dominant Provider shall send to the Director and to every Third Party with which it has entered into an Access Contract covered by Condition C1 a written notice of any amendment to the charges, terms and conditions on which it provides Network Access or in relation to any charges for new Network Access (an "Access Charge Change Notice") not less than 90 days before any such amendment comes into effect.

C4.3 The Dominant Provider shall ensure that an Access Charge Change Notice includes:

- (a) a description of the Network Access in question;
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- (b) a reference to the location in the Dominant Provider's current Reference Offer of the terms and conditions associated with the provision of that Network Access; and
- (c) the date on which or the period for which any amendments to charges, terms and conditions will take effect (the "effective date").

C4.4 The Dominant Provider shall not apply any new charge, term and condition identified in an Access Charge Change Notice before the effective date.

C4.5 To the extent that the Dominant Provider provides to itself Network Access that:

- (i) is the same, similar or equivalent to that provided to any other Third Party; or
- (ii) may be used for a purpose that is the same, similar or equivalent to that provided to any other Third Party,

in a manner that differs from that detailed in an Access Charge Change Notice in relation to Network Access provided to any other Third Party, the Dominant Provider shall ensure that it sends to the Director an Access Charge Change Notice in relation to the Network Access that it provides to itself which includes, where relevant, at least those matters detailed in Condition C4.3(a)-(c).

Condition C5 – Requirement to notify technical information

C5.1 Save where the Director consents otherwise, where the Dominant Provider:

- (a) proposes to provide Network Access covered by Condition C1, the terms and conditions for which comprise new:
-

- (i) technical characteristics (including information on network configuration where necessary to make effective use of the Network Access);
- (ii) locations of the points of Network Access; or
- (iii) technical standards (including any usage restrictions and other security issues),

or

- (b) proposes to amend an existing Access Contract covered by Condition C1 by modifying the terms and conditions listed in paragraph C5.1 (a) (i) to (iii) on which the Network Access is provided,

the Dominant Provider shall publish a written notice (the 'Notice') of the new or amended terms and conditions not less than 90 days before either the Dominant Provider enters into an Access Contract to provide the new Network Access or the amended terms and conditions of the existing Access Contract come into effect.

C5.2 The Dominant Provider shall ensure that the Notice includes:

- (a) a description of the Network Access in question;
- (b) a reference to the location in the Dominant Provider's Reference Offer of the relevant terms and conditions; and
- (c) the date on which or the period for which the Dominant Provider may enter into an Access Contract to provide the new Network Access or any amendments to the relevant terms and conditions will take effect (the "effective date").

C5.3 The Dominant Provider shall not enter into an Access Contract containing the terms and conditions identified in the Notice or apply any new relevant terms and conditions identified in the Notice before the effective date.

C5.4 Publication referred to in paragraph C5.1 shall be effected by:

- (a) placing a copy of the Notice on any relevant website operated or controlled by the Dominant Provider;
 - (b) sending a copy of the Notice to the Director; and
 - (c) sending a copy of the Notice to any Third Party at that Third Party's written request, and where the Notice identifies a modification to existing relevant terms and conditions, to every Third Party with which the Dominant Provider has entered into an Access Contract covered by Condition C1. The provision of such a copy of the Notice may be subject to a reasonable charge.
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Annex B

Representations received

Table B.1 Non-confidential representations on August 2003 Notification & Explanatory Statement

Consultation respondent	Oftel market definition proposal: for or against	Oftel SMP proposal: for or against overall conclusion
Kingston	No comment	Disagree
European Commission	Agree	No comment
BT	No comment	Agree
Total (also taking account of last consultation)	1 For 0 Against 2 No specific comment	1 For 1 Against 1 No specific comment

Annex C

Responses to comments on market definition

Retail market definition

C.1 Comments were received in relation to Of tel's critical loss analysis, demand-side substitution, consumer reactions to a 10% price increase, and market definition in the absence of regulation.

Critical loss analysis

C.2 One respondent makes several comments on Of tel's estimation of the critical loss factor:

- A wide range for the critical loss factor is not meaningful for market definition.
- The range is not weighted by probability analysis. The respondent advocates weighting each significant price point (between £13 and £17, the typical residential prices on offer) to reflect the number of consumers that are present at each price point. This would reduce the estimate range presented by Of tel and produce a robust result.
- Marginal costs facing the hypothetical monopolist would be lower than the range proposed by Of tel, since Of tel has essentially used costs which an ISP entering the market would face rather than those faced by the hypothetical monopolist.
- The sales and marketing savings will be less than those proposed by Of tel.
- The respondent concludes that a reasonable estimate for the critical value for residential consumers would be 12.9% to 16.7%.

C.3 As outlined in Annex A in the consultation document, estimation of the critical loss facing the hypothetical monopolist is based on a number of key assumptions, namely the initial price of the retail unmetered Internet product and the marginal cost saved per unit of volume increase facing the hypothetical monopolist. Of tel used market information to estimate the value of these inputs. As a result the range of estimates for the critical loss factor reflects the possible range for these inputs.

C.4 The initial price of the retail unmetered Internet product for residential consumers reflects the range of prices currently offered by suppliers of the retail product. These were outlined in Table 3 of Annex A in the consultation document. The business tariff reflected the average monthly price paid by SMEs, based on Of tel survey data.

C.5 The marginal cost estimate was based on the costs to a hypothetical monopolist of a port of an unmetered Internet termination and the contention ratio employed by the hypothetical monopolist. As noted in the consultation document Of tel has found that the cost of an unmetered Internet termination port varies

according to the number of ports purchased and the length of contract undertaken. Therefore a range of prices were used in the analysis. Finally on the basis of evidence from industry Oftel has assumed that contention ratios are 10:1 for residential services and 4:1 for business services.

C.6 On the basis of this it seems reasonable to Oftel to produce a range of estimates for the critical value facing a hypothetical monopolist. Oftel has not weighted the range of estimates because the results are simply interpreted as indicative of market boundaries. Oftel does not believe that weighting each significant price point between the current range of prices available to consumers would make the estimate of the critical value any more robust.

C.7 Oftel accepts that the appropriate marginal cost savings facing the hypothetical monopolist may be lower than that proposed in the consultation document. For the purposes of the consultation Oftel used market prices of a range of products available to service providers entering the market. However since the hypothetical monopolist would serve the whole market it seems likely that economies of scale could be achieved. Hence the marginal costs facing the hypothetical monopolist are likely to be lower than those facing an ISP. The respondent suggests that marginal costs would fall in the range of £45-55.

C.8 Using this range Oftel estimates critical values of 12% to 15% for residential users and 12% to 13% for business users.

C.9 Oftel's survey data showed that 7% of residential users of narrowband unmetered services claimed that they would switch to metered services as a result of a 10% price increase. 14% of business users of unmetered services would switch to metered services in response to a 10% price increase.

C.10 The residential results are clearly lower than the critical value estimates, although the business result appears to slightly exceed the critical value estimates.

C.11 The same survey showed that 14% of residential users of narrowband unmetered services would consider switching to broadband services (7% to lower speed and 7% to higher speed broadband internet access) as a result of a 10% price increase. 3% of business users of unmetered services would switch to broadband services in response to a 10% price increase.

C.12 The business result is substantially lower than the critical loss estimate although the residential result is not conclusive.

C.13 The revised critical loss estimates do not have a substantial impact on Oftel's conclusions. The only result to have changed (relative to the critical loss estimate) is the apparent substitutability between unmetered and metered Internet services for business users. However Oftel believes that the results are still consistent with a distinct unmetered Internet access market for the following reasons:

- The calculation is relatively conservative because Oftel's previous market research has found that fewer customers actually switch than claim they would switch services. Therefore the survey results are expected to be over-estimates of switching behaviour. Moreover the result is based on the assumption that all consumers would instantly switch whereas in reality they would switch over time.
- Oftel does not rely solely on the SSNIP test to define the market boundaries. They are used to complement consumer survey information on usage patterns and the reasons why consumers use particular packages, as set out in Annex A of the August consultation document.

Demand-side substitution

C.14 The Commission notes that "Oftel's analysis of demand-side substitution would have been stronger had it been based on a broader empirical foundation, as there could be high churn rates between metered and unmetered services".

C.15 Oftel did consider the degree of switching between metered and unmetered services in the consultation document (paragraph A.35), outlining the reason why churn rates are not useful indicators of demand side substitutability (paragraphs A.45-A.47). As a result Oftel used critical value estimates and survey evidence about willingness to switch to other services in response to price rises to inform the analysis of market boundaries. In addition Oftel considered survey evidence about the reasons why consumers use unmetered Internet services (paragraphs A.41 and A.56).

Consumer reactions to a 10% price increase

C.16 One respondent is critical of the way Oftel assesses whether a hypothetical monopolist can profitably increase prices, arguing that the correct approach is to consider the total number of people who would switch out of unmetered internet services, thereby placing a constraint on the pricing of the hypothetical monopolist. The respondent argues that this is the correct approach given that the hypothetical monopolist would be indifferent about where its customers switch and would only be concerned about whether or not the price rise were profitable. Rather than considering whether pairs of products are sufficiently good substitutes to be subject to a common pricing constraint, this would give an indication of whether the pricing behaviour of the hypothetical monopolist is constrained by switching to all substitutes together.

C.17 In the August consultation document the potential for demand side substitution between unmetered and metered Internet use and unmetered Internet and broadband use is considered. Separate analyses are undertaken for business and residential use.

C.18 First the Director considered whether residential (and business) users of unmetered Internet services would consider switching to metered Internet use in response to a 10% price increase and then whether residential (and business) users of unmetered Internet services would consider switching to broadband services in response to a 10% price increase.

C.19 If the approach to the hypothetical monopolist test suggested by the respondent is applied to the survey evidence of consumer switching intentions then it might appear that unmetered narrowband services are not a separate market. However, Oftel believes that it would be wrong to place so great a weight on survey evidence of this nature because the level of claimed switching intentions is rarely achieved in practice. In addition, other evidence emphasises the importance to consumers of the qualitative differences between metered and unmetered narrowband and broadband services. Moreover, the markets for Internet access services are still evolving and liable to change over time.

C.21 One of the weaknesses of relying on the available empirical data to carry out the SSNIP test is that the markets for narrowband and broadband Internet access are still evolving and switching may reflect factors other than a pure price response by consumers. For example it is feasible that consumers have and will migrate from unmetered to broadband services as they become aware of the relatively new broadband services, attracted by the particular features of broadband services. Moreover it is likely that some will change their mind if, say, the specific features of broadband access do not suit them as well as initially thought.

C.22 As a result the analysis of market definition should consider other sources of evidence such as the features of unmetered and other forms of access valued by consumers, patterns of use and so on.

C.23 Oftel's definition of three separate markets, metered, unmetered and broadband services, reflects the different characteristics of the services and survey evidence which suggests that large numbers of consumers value the characteristics of these distinct services.

C.24 Oftel therefore believes that it should continue to define separate markets for metered and unmetered narrowband and for broadband services. The empirical evidence to support a wider market definition as proposed by the respondent is inconclusive. However, if the market were widened then the data would suggest that it would be broadened to include broadband services, i.e. the nearest demand side substitute. It is unlikely that a further SSNIP test on this wider market would suggest that it should be broadened to include metered internet access services. Thus, adopting the respondent's proposed approach might lead to broadband (but not metered narrowband) being considered in constraints on unmetered

narrowband¹. At this point, it is worth re-iterating that market definition is a means to an end, which is to assess the extent of competition in the relevant market. In the context of this market review the aim is to assess the need for regulation to protect consumers. Thus the key question for Oftel, if it adopted this wider market definition, would be whether there would be a high risk that consumers of unmetered narrowband services would not be adequately protected simply by the availability of broadband. Oftel believes that there would indeed be a high risk of this. This is particularly true given the fact that prices of broadband are not currently regulated. Therefore Oftel considers that, even if a wider market were defined, it would reach the same conclusions regarding remedies as with its preferred definition of separate markets.

Market definition in the absence of regulation

C.25 One respondent argues that if retail markets were defined in the absence of wholesale regulation no unmetered retail product would exist and the natural conclusion would be that there would just be a narrowband Internet access market.

C.26 Oftel disagrees with this perspective. Oftel's analysis of markets is consistent with the existence of FRIACO because FRIACO regulation is imposed on the wholesale call origination market (in response to competitive conditions at this level) rather than at the wholesale Internet termination level. The principle of defining markets in the absence of wholesale regulation refers to wholesale regulation in the wholesale market being considered, ie in the absence of a wholesale unmetered termination product being available on regulated terms, rather than the absence of any wholesale market regulation at all. It does not preclude the supply of a wholesale unmetered narrowband Internet termination product by the hypothetical monopolist or the existence of an unmetered retail product.

Wholesale market definition

C.27 One respondent argues that Oftel should not rigidly rely on the derived demand approach to inform wholesale market boundaries. Demand and supply-side substitutability at the wholesale level should also be considered in terms of the characteristics of the wholesale market. In addition the Commission noted that unmetered wholesale services, like FRIACO, could be used for retail services other than just unmetered Internet access.

¹ Note that even if a wider market were adopted here, this would not necessarily mean that broadband services would be part of a wider market when considered from the perspective of Wholesale Broadband Access market review. The analytical question in that market review applies to switching behaviour of broadband consumers rather than switching behaviour of unmetered narrowband consumers. This issue will be considered in the Wholesale Broadband Market Review.

C.28 Oftel outlined the logic behind the approach to market definition in paragraph A.41 of the consultation document.

C.29 Oftel accepts that unmetered wholesale services can in principle be used for a number of retail services. However, the effect of this on demand conditions at the wholesale level would still be considered in the context of looking at demand derived from the retail level. Moreover Oftel is not aware that this is currently widespread in the UK. As a result it is not expected that including the full range of uses of unmetered wholesale services would alter the analysis outlined in the consultation document dramatically.

C.30 In fact Oftel has effectively considered the extent of demand-side substitutability at the wholesale level by assessing the nature of supply-side substitutability at the retail level. In other words the two are equivalent. This follows since wholesale services are used to provide retail services. Hence the main driver of demand side substitutability at the wholesale level would be conditions at the retail level.

C.31 For example in order to consider whether demand for wholesale metered services would constrain the pricing behaviour of a hypothetical monopolist supplier of wholesale unmetered services it is necessary to consider the extent to which purchasers of wholesale unmetered services would switch to wholesale metered services in response to a price increase. If ISPs were able to substitute a metered wholesale product for an unmetered wholesale product in order to supply an unmetered retail product to consumers the pricing behaviour of the hypothetical monopolist at the wholesale level may be constrained. This was considered in the consultation document in terms of the extent to supply-side substitution at the retail level. In other words the extent to wholesale demand-side substitutability at the wholesale level depends on the nature of supply-side substitutability at the retail level. This was outlined in the consultation document in paragraphs A.59 to A.62.

C.32 Therefore, Oftel's derived demand approach is consistent with the observations made by the European Commission and the other respondent.

Annex D

Discontinuation Notice

NOTICE TO KINGSTON COMMUNICATIONS (HULL) PLC UNDER PARAGRAPH 9 OF SCHEDULE 18 TO THE COMMUNICATIONS ACT 2003

Notice that certain continued provisions set out in the continuation notice given to Kingston Communications (Hull) plc on 23 July 2003 will cease to have effect from the date this notice is deemed to be effected in accordance with section 7 of the Interpretation Act 1978 and section 394(7) of the Communications Act 2003

1. The Director General of Telecommunications ('the Director'), in accordance with Paragraph 9(9) of Schedule 18 to the Communications Act 2003 ('the Act') hereby gives notice to Kingston Communications (Hull) plc ('Kingston') that certain continued provisions contained in Schedule 1 to the continuation notice given to Kingston on 23 July 2003, which had effect from 25 July 2003, ('the Continuation Notice'), will cease to have effect from the date this notice is deemed to be effected in accordance with section 7 of the Interpretation Act 1978 and section 394(7) of the Communications Act 2003, to the extent set out in Schedule 1 to this notice ('the Discontinued Provisions').

2. In giving this notice, the Director has, in accordance with Paragraph 9 (11) of Schedule 18 to the Act, taken all steps necessary for enabling him to decide whether or not to set a condition under Chapter 1 of Part 2 of the Act for the purpose of replacing the continued provisions and whether or not to exercise his power to set a condition under that Chapter for that purpose.

3. All directions, determinations, consents and other provisions which were continued under the Continuation Notice by virtue of Paragraph 9(8) of Schedule 18 to the Act will also cease to have effect from the date this notice is deemed to be effected in accordance with section 7 of the Interpretation Act 1978 and section 394(7) of the Communications Act 2003, to the extent that they were given or made for the purposes of the Discontinued Provisions.

4. To the extent that the Continuation Notice does not cease to have effect under Paragraph 1 of this notice, the Continuation Notice shall continue to have effect until the Director has given a further notice to Kingston in accordance with Paragraph 9(9) of Schedule 18 to the Act that it shall cease to have effect.

5. The Director issued a consultation as to his proposals to discontinue the Discontinued Provisions on 2 October 2003 and requested comments by 9.00a.m.

on 16 October 2003. The Director has taken into account the comments he received during that consultation.

6. In this notice, except as otherwise provided or unless the context otherwise requires, words or expressions shall have the meaning assigned to them and otherwise any word or expression shall have the same meaning as it has in the Act. For the purposes of interpreting this notice, headings and titles shall be disregarded.

DAVID ALBERT EDMONDS
DIRECTOR GENERAL OF TELECOMMUNICATIONS]

Date 27 November 2003

Schedule 1

The following continued provisions which were contained in Schedule 1 to the Continuation Notice will cease to have effect from the date this notice is deemed to be effected in accordance with section 7 of the Interpretation Act 1978 and section 394(7) of the Communications Act 2003, to the extent set out below.

Condition 43 in so far as the condition relates to the market which has been reviewed in the *wholesale unmetered narrowband Internet termination services - Hull area* market review ('the Market Review'), and which will be replaced by SMP Conditions imposed on Kingston by way of the Notification set out in Annex A of the Market Review published by the Director on 28 November 2003.
