Ofcom's Business Connectivity Market review

Virgin Media response

11 February 2019

Non-Confidential Response

Contents

Executive Summary

Virgin Media welcomes the opportunity to respond to this consultation. We believe that Ofcom's approach to this Business Connectivity Market Review, its provisional findings, and the remedies proposed are generally appropriate. They reflect the fact that this is a bridging review, applying to a shorter period than would otherwise be the case: this is not a review via which new or innovative approaches to regulation should be introduced.

This review is a component and facilitator of Ofcom's over-arching programme aimed at the establishment of regulatory certainty to support long-term fibre investment. We are very strong advocates of this programme and encourage Ofcom to take the bold decisions that will be necessary for its aims – and ultimately the benefits for consumers - to be realised.

It is important that Ofcom considers the specific elements of this review, and its role, holistically, alongside the other elements of the programme. These include the Passive Infrastructure Market Review and the consultation on the approach to geographic markets, both of which share common aspects with it.

We believe that the proposals set out in this review are, in general, consistent with Ofcom's stated objective to incentivise and support investment in competing infrastructure. These include:

- Recognising different competitive areas within the UK;
- Recognising that different competitive conditions can exist within a market;
- Proposing remedies that reflect those different conditions;
- Recognising different approaches for different products within a market;
- Adopting a cautious approach to regulation in areas which may be opened up to competition under DPA proposals.

This is very welcome and we applaud Ofcom for staying true to the intentions set out in its Strategic Policy Position of July 2018. However, there are a several specific aspects that risk, in our view, having the opposite effect.

In particular, we are concerned that the proposed imposition of a dark fibre remedy is premature and risks having a disincentive effect on the prospects of investment. We do not believe that a short term, bridging review is the correct mechanism via which to introduce a fundamentally new regulatory remedy – and even if it was, Ofcom has not taken sufficient account of the prospect of competitive entry in the areas in which it would be available. We propose alternative approaches that we consider would allow Ofcom to consider the matter in the wider, longer term context and that would have a less damaging effect on investment.

Introduction

Regulation of the Business Connectivity Markets is a vitally important task for Ofcom. Regulation needs to encourage competition developing through investment whilst providing appropriate and proportionate protection against Openreach from abusing any dominance it may hold as a result of its ubiquitous network presence, and stifling competition and the prospect of competition from other networks, including Virgin Media.

The markets under review cover the provision of leased lines, which are the backbone of this country's connectivity, providing direct data links to businesses, medium and large enterprise and public sector organisations, and enabling the provision of residential services by connecting CPs' networks to the 'final mile' access legs provided by Openreach. The importance of getting the right regulation in these markets cannot be understated.

Virgin Media Business has both a large direct and indirect leased line business. It provides base connectivity to wholesalers and resellers and utilises leased lines in larger more complex network deployments to enterprise and government customers. As the major infrastructure owning competitor to BT, it provides services on both an on-net and off-net basis to all of our customers. Virgin Media is committed to investing to expand its network which brings benefits to both residential and business segments, we therefore have a strong interest in these markets working fairly and efficiently to support this continued investment, growth and expansion.

Virgin Media strongly agrees with Ofcom's clear intention, as set out as the title to its Executive Summary, to ensure that regulation supports long-term fibre investment. It is vital that regulation supports and encourages alternative network investment (alongside continued investment by Openreach) to ensure that the UK has the right communications infrastructure to serve businesses and in turn support the UK's economic future.

We set out our views below on the issues raised in the consultation, grouping our comments in the same order as the questions posed by Ofcom. We have included the questions that we respond to in our response at the start of each section for ease of reference.

Contemporary Interface (CI) Access – Product Market Definition

Question 4.1: Do you agree with our proposed approach to product market definition? Please provide evidence to support your views.

Question 4.2: Do you agree with our proposed CI Access product market definition? Please provide evidence to support your views.

Ofcom proposes to define a single market for all bandwidth products; this is a departure from currently imposed regulation in these markets[1]. In 2013, Ofcom defined markets[2] at 1Gb and below and at above 1Gb or any bandwidth WDM service. This recognised the different nature of both the use to which the products were put and the different customer groups that purchased these products.

In 2016, Ofcom introduced a single bandwidth market for all CI products because it found a chain of substitution between the two markets. This decision was subsequently reviewed on appeal, and the Competition Appeal Tribunal found that Ofcom had erred in its determination of the relevant product market and remitted the matter back to Ofcom.

As the consultation sets out, temporary regulation is currently in place that regulates only the 1Gb and below market, and this review re-examines the issue of product market afresh.

Ofcom notes that the market has moved on since its analysis that led to the 2016 statement.

Demand Side Analysis

Ofcom examines demand side substitution in its analysis of what services may sit within the same product market. This was the approach that was taken in 2016, and therefore the comments made by the CAT in relation to the errors made by Ofcom remain relevant. However, Ofcom concedes that the evidence is ambiguous with respect to the presence of a separate VHB market from the demand side[3], and therefore looks to other evidence to determine its proposed product market.

Ofcom therefore, places greater reliance on supply side substitution to support its proposed product market definition.

Supply Side Analysis

Ofcom considers supply side substitution in the context of a rival CP having an existing connection to a customer (i.e. where no additional construction work will be required) and where a rival CP has to dig to connect to a customer.

[1] Current BCMR Temporary Conditions which define a market for circuits at 1Gb and below.
[2] Excluding separate TI markets
[3] Consultation paragraph 4.32

In the former, Ofcom provisionally concludes that the relatively low cost of electronic equipment means that there would be supply side substitution, as even where different electronic equipment would be required in order to provide a higher speed service (in some cases the same equipment will facilitate different bandwidth services), the cost of provision will be relatively low.

In the latter case, Ofcom suggests that the key issue is whether CPs would behave differently towards digging when providing services of different bandwidths. Although Table 4.2 suggests that the economic dig distances for different CI Access services vary considerably[4], Ofcom prefers to rely on actual data supplied in relation to dig distances. This suggests that there is very little digging by other CPs, irrespective of bandwidth, and the actual dig distances for 2017 are very similar for 1Gb and VHB services, with the median distance being slightly higher (20m) for 1Gb compared to VHB (17m). Virgin Media notes that the number of VHB digs taken into account is extremely small (17) and therefore it is unlikely to be representative of all commercial opportunities in VHB services; it is likely to be attractive to dig further for the higher return that is available on VHB products.

Overall, Virgin Media considers that Ofcom's analysis of the product market arrives at a justifiable conclusion, but we believe that it must consider additional evidence to ensure that its final decision can withstand scrutiny. We consider that there have been developments in the market since Ofcom's last review that suggest there is a narrowing between 1Gb and VHB products – and which support demand side substitution as well as supply side substitution described above (and hence the definition of a single all-bandwidth market). However, despite this increased substitutability, we observe that some differences in the levels of competitiveness within the market remain. While this may not be sufficient to justify the definition of separate markets, we do believe that the differences must be acknowledged in the approach taken by Ofcom. To that end, we support Ofcom's proposed imposition of different remedies for 1Gb and below products compared to VHB products.

We also note that Ofcom has undertaken a sensitivity analysis in assessing separate markets for 1Gb and VHB services, finding that BT would have SMP in both markets in any event. In this regard, it is likely that the practical effect of a single or separate markets is academic, meaning that there is little risk in defining a single market.

[4] Consultation Table 4.2: economic dig distance based on 3-year payback will be 27m for 100Mb; 43m for 1Gb and 95m for 10Gb services.

Contemporary Interface (CI) Access – Geographic Market Definition

Question 5.1: Do you agree with our proposed approach to geographic market analysis for CI Access? Please provide evidence to support your views.

Question 5.2: Do you agree with our proposed definition of geographic markets for CI Access? Please provide evidence to support your views.

Virgin Media considers that sub-national geographic markets have increasing importance within the CI Access markets, especially in the context of ensuring that Ofcom's primary objective of supporting long term infrastructure investment is met.

We agree with Ofcom that levels of competition in different areas of the country will vary depending on the presence or potential future presence of non-Openreach providers. An area that is remote, where it is not realistic for any non-Openreach network build to occur, will require different treatment to an area with other provider present.

Ofcom proposes to use its Network Reach analysis to determine the level of competition in a given postcode sector. We agree with Ofcom that to try to analyse competition on a more granular level is unlikely to be practical, although we consider that close attention needs to be paid to the indicative competitive conditions in Metro Areas.

Ofcom also proposes to adjust the buffer distance from their previous 2016 analysis from 100m down to 50m. Essentially, this means that a provider will not be able to supply competitively a business customer if its existing network is further than 50m away from the premises. Virgin Media does not consider that this is an appropriate buffer distance to use. At the very least, a 100m buffer test should be maintained. We set out below our use of 100m in Virgin Media's decision making process about build decisions, and provide evidence that a significant number are of distances in excess of 50meters[5].

Ofcom already sets out in Section 4[6] that the economic dig distance for VHB services is between 95 and 120m, for 1Gb between 43 and 69m and for 100Mb between 27 and 47m based on 3 and 5-year payback periods. This suggests that 'economically rational' digging would be well in excess of the 50m buffer distance for 1Gb and above (over a 5 year payback period), and even for 100Mb, 47m is very close to the theoretical limit chosen by Ofcom.

Ofcom notes that it has conducted a sensitivity analysis based on 100m dig distance, and as set out in Annex 13, the conclusions do not change. Notwithstanding this, Virgin Media considers that 100m is the minimum appropriate distance and sensitivities should be conducted at 50m and 150/200m. To take the approach proposed risks understating the competitive conditions in some areas, which

[5] See response to Question 7 below.
[6] Consultation Paragraph 4.57 and Table 4.2

in turn could have serious implications on Ofcom's intention to ensure long term investment incentives are maintained.

Ofcom suggests that a 25m buffer distance could be appropriate based on actual dig data collected[7], however, this again ignores actual economic incentives as to what may be possible.

Ofcom has also not considered, in its economic assessment of dig distances, the prospect of a customer initially taking a service of a certain bandwidth, and then upgrading that bandwidth during the lifetime of the contract. When considering contract value, it can be relevant to include the potential value of an in-life upgrade which would make a longer dig distance than those set out in table 4.57 appropriate.

Virgin Media agrees with Ofcom that BT Only, BT+1 and HNR areas should be treated as separate geographic markets for the purpose of regulation. We consider that all three areas have distinct competitive characteristics. We also agree with Ofcom's approach to define 11 geographic markets as set out in paragraph 5.52, with six city based geographic markets, and a separate "other HNR" market alongside, CLA, BT Only, BT+1, and Hull markets.

[7] Consultation paragraph 5.21

Contemporary Interface (CI) Access – SMP Analysis

Question 6.1: Do you agree with our proposed approach to SMP assessment for CI Access in the UK excluding the Hull Area? Please provide evidence to support your views.

Question 6.2: Do you agree with our proposed SMP findings for CI Access in each of the geographic markets defined? Please provide evidence to support your views.

Ofcom provisionally concludes that Openreach holds SMP in all identified markets save for the CLA, which is provisionally assessed as competitive. We discuss the proposals in more detail below, but we note that Ofcom has acknowledged the differing competitive conditions within an SMP market in its approach to remedies; we consider this to be both correct and essential to ensure that the overall intention of promoting network investment is maintained.

Ofcom has assessed service share data based on 2017 connections rather than a full circuit inventory. We note that the circuit inventory data has been used as a sensitivity and does not alter the assessment or proposed SMP findings.

We note that Ofcom has relied on the results of the 2016 BDRC survey to support some of their analysis in relation to SMP[8]. We would caution the overreliance on this data given the extremely small sample size, both overall, and in relation to sub-categories of customer. Whilst it does suggest that common sense factors such as positive commercial relationships with suppliers will be relevant in a switching decision, Virgin Media considers that the information presented in the survey should not be regarded as significant or conclusive of any trend in itself.

We agree that Ofcom is correct to ensure that future network expansion plans should be taken into account.

Overall we consider that Ofcom is correct to propose the SMP findings it has set out in the consultation.

[8] Consultation paragraph 6.62/6.63 in relation to choice of supplier / switching

CI Inter-exchange connectivity

Question 7.1: Do you agree with our assessment of inter-exchange connectivity? Please provide evidence to support your views.

Question 7.2: Do you agree with the proposed market definition? Please provide evidence to support your views.

Question 7.3: Do you consider that our list of BT exchanges for de-regulation is correct? Please provide evidence to support your views.

Question 7.4: Do you agree with our list of Principal Core Operators (PCOs)? Please provide evidence to support your views.

Virgin Media agrees that a revised approach to regulation of the market for "from the exchange" connectivity is appropriate. Ofcom has sought to differentiate access connectivity to the exchange, and onward connectivity from that exchange, by proposing separate markets. We agree that the focus of regulation should be on inter-exchange connectivity.

We agree with the designation on PCOs and agree with Virgin Media's inclusion on that list. We do not comment on the inclusion or omission of other CPs.

We wholly agree with Ofcom's proposal to treat direct and indirect exchange connectivity in the same way. Cablelink is a regulated product and allows for exchange connectivity as much as direct connectivity. Virgin Media already makes use of external Cablelink to provide exchange connectivity to customers, and to have treated this type of connectivity in a different way could have had a potentially significant effect on this market if it resulted in more exchanges being included in the "BT Only" category.

We do submit that Ofcom has not sufficiently considered the prospect of networks deciding to connect to new exchanges. Ofcom suggests that this is accounted for in its analysis at paragraph 7.60, but then dismisses this effect due to the average distance from the exchange groupings of BT only[9] and BT+1[10].

Virgin Media considers that there are a significant number of additional exchanges where it would be economic for us to extend our network to provide exchange backhaul via an external Cablelink connection. The demand would arise from a CP who wished to have non-BT backhaul from the exchange. As noted by Ofcom, this is a market that Virgin Media leads, and therefore it is possible that we could connect these exchanges. Ofcom states that there is an absence of confirmed plans, however, this misses the point of demand-driven business network expansion; if a request was made in relation to one of these exchanges we would provide the service, and therefore these [✂]

[9] Consultation paragraph 7.64
[10] Consultation paragraph 7.69

exchanges should be included in the BT+1 market. We have detailed the exchanges that we consider should be included in this market at Annex 1 to our response.

In order to derive this list we have analysed our network exchange proximity and also looked at the potential number of businesses in the area that could be served if network was extended to that exchange.

Profile of proposed in-scope BTEs by prospect density and proximity to VM Network

[✂]

This table shows that [✂] exchanges exist within the proposed BT Only market that sit within 100m of the Virgin Media network, the majority of which would provide access to areas with over [✂] potentially addressable businesses from that exchange and over a third providing potential access to up to between [✂] businesses[11].

Although the network is within 100m of these exchanges, it is also important to consider the economic incentive to dig. As set out above, Ofcom has suggested that networks are unwilling to dig over any substantive distance, irrespective of the theoretical economic justification for doing so. Virgin Media disagrees with this proposition. We have looked at both our general business practices and also specific contracts to illustrate that considerably longer distances will be dug if the deal is worth pursuing. We consider the following issues support our arguments:

1. **Internal Contract Tools**

Our internal pricing tools are set to consider [✂] dig distances for basic Ethernet connectivity contracts. This distance has been set based on our experience of providing such services, with [✂] being a reasonable limit for non-VHB services, taking account of relevant factors such as the probability of encountering obstacles when digging longer distances.

An analysis of 2018 data from our Business Pricing Tool shows the following:

[11] The more potential businesses near an exchange will also provide prospects for business connectivity solutions to be offered on a combination of "on-net" backhaul from an exchange and off-net "local access" variant connectivity purchased from Openreach even without any additional construction to those businesses.

[✂]

Of the [✂] circuits ordered [✂] circuits had a dig distance of between 50 and 100m. This is a significant number of circuits, representing over [✂] % of all orders for the year. The percentage value increases for sites quoted. Of the [✂] sites quoted, over [✂] % were associated with dig distances of between 50 and 100m. The fact that quote was provided shows that it was viable for that dig to be undertaken in those cases.

2. Specific Contract Examples

The generic pricing tools use a [✂] limit for practical purposes to ensure that appropriate "Business As Usual" circuits are quoted for appropriately however, this does not mean that longer dig distances will not be undertaken by Virgin Media Business where justified by the value of the prospective business.

[✂]

This contract is not unique and the experience of digging considerable distances (and considerably over 100m) [✂].

Therefore, Virgin Media does not recognise the 17m distance quoted for VHB connectivity as being either representative or something that should be relied upon to determine that an exchange should fall within the BT Only market.

To take that approach, Ofcom is essentially relying on a snapshot of connectivity from the time of its last information request submission. This is not the way that a market review should be undertaken. Market Reviews are a forward-looking exercise and should consider the market conditions based on the potential for competition over the future period. We also consider that our information discussed above is based on the current competitive environment, and therefore does not include the additional competitive opportunities that may be afforded through the proposed DPA remedy which sits upstream of these markets. The latter can only increase competitive opportunities during this review period.

Virgin Media agrees with the SMP assessment of Ofcom that the BT+2 market is competitive. Ofcom suggests that the BT+1 market, where the +1 is Virgin Media, will also not be competitive as Virgin Media is incentivised to price its wholesale services uncompetitively to CPs who are also competitors at the retail level.

We do not agree with this assertion. Purchasers of exchange backhaul from Virgin Media will purchase this type of connectivity on the basis of a much larger contract with services being provided from a large number of exchanges. The buyer power that such a customer exerts and the fact that connectivity will be provided from a significant number of competitive BT+2 exchanges, will mean that Virgin Media will be required to price at a competitive level across all exchanges in order to secure the contract.

Therefore, the competitive conditions for BT+1 areas should not be considered as if there is no competition (akin to BT Only areas), and we consider that the provisional conclusion in finding BT to hold SMP in BT+1 areas has not been fully considered by Ofcom. Even if a finding of SMP is justified on the evidence, the competitive conditions in a BT+1 market compared to the BT Only market are significantly different, giving rise to different competition concerns and justifying a wholly different approach to remedies.

Traditional interface (TI) services

Question 8.1: Do you agree with our proposal not to regulate the low bandwidth TI services market on the basis that it no longer fulfils the three criteria test set out in the European Commission Recommendation? Please provide evidence to support your views.

Virgin Media agrees with Ofcom that the TI market no longer meets the three criteria test, and that as such Ofcom's proposal to remove regulation is correct in those circumstances.

Hull Area

Question 9.1: Do you agree with our proposal to deregulate the retail market for CI services at all bandwidths in the Hull Area? Please provide evidence to support your views.

Question 9.2: Do you agree with our analysis and proposed findings in relation to the wholesale market for CI Access services at all bandwidths in the Hull Area? Please provide evidence to support your views.

Question 9.3: Do you agree with our proposal to deregulate wholesale TI services at all bandwidths in the Hull Area? Please provide evidence to support your views.

Virgin Media has no comment in relation the to the proposed regulation of the Hull Area

Approach to remedies

Question 10.1: Do you agree with our proposed approach to remedies? Please provide reasons and evidence in support of your views.

Ofcom summarises its principles in paragraph 10.6 as:

- Promoting network based competition, targeting our regulation upstream to passive network infrastructure;

- Removing regulation where competitive conditions allow; and
- Protecting customers by regulating where necessary.

Virgin Media strongly agrees that these key principles should underlie the regulation of the business connectivity markets and the imposition of remedies on markets where Ofcom proposes BT holds SMP.

We also agree with Ofcom's provisional assessment that competitive conditions will evolve, especially in light of the passive access remedy, DPA, becoming unrestricted. Therefore, Ofcom has to consider very carefully where regulation should be imposed for consumer protection purposes on the basis that investment is unlikely[12]. Ofcom's approach to ensure that where there is the potential for greater competition there should be "an objective to create the right conditions for network builders to invest with confidence", which would be achieved by the use of lighter regulation in these areas[13].

Ofcom notes that DPA may take time to bring competition to currently uncompetitive areas[14], but that this does not mean that competition will not develop. The DPA product must be allowed time to realise its full potential. To do otherwise would be inconsistent with the considerable effort that Ofcom has invested in its development – and could be seen as a lack of faith in its utility. We therefore welcome Ofcom's recognition of the potential of DPA and its approach to differentiate DPA prospect areas from areas where competition is least likely to develop, even in light of DPA. We note that the approach to dark fibre is based on the remedy only being made available in this latter category of entrenched uncompetitiveness. We discuss Ofcom's approach to dark fibre in more detail below.

Virgin Media agrees with Ofcom's approach to differentiating remedies based on the level of competition or prospective competition in a market, and accordingly proposing lighter remedies for the HNR / Metro Areas than for other CI Access areas.

We agree also with Ofcom's approach to pricing, in that the cap for currently charge controlled products will be sufficient to keep prices close to cost (bearing in mind the transitional nature of this two year review period prior to access regulation being brought together), and the imposition of a safeguard cap on the commercially priced higher bandwidth services that are likely to provide a focus for initial competition in the market, through DPA, which will act as a more natural constraint on pricing.

[12] Consultation Paragraph 10.7 : approach to remedies summary
[13] Consultation Paragraph 10.10
[14] Consultation Paragraph 10.11

General remedies

Question 11.1: Do you agree with the general remedies that we propose? Please provide reasons and evidence in support of your views.

Virgin Media broadly agrees with Ofcom's approach to the proposed general remedies. The remedies themselves are well established and understood conditions that have been imposed on BT in SMP markets over a number of review cycles. Where SMP has been found they provide an appropriate base for the regulation of BT, and we agree that they are appropriate recognising and supporting the variation Ofcom identifies between different markets. It is vitally important that familiar regulation should not be imposed simply because it "has always been there". Virgin Media notes the proposal to align the SOR process with the WLA conditions, in order to reflect the intention to align the BCMR and WLA reviews in the next cycle. This appears to be an appropriate step in line with Ofcom's longer intent.

Specific dark fibre remedy for inter-exchange connectivity

Question 12.1: Do you agree with the aims and effect of our proposed dark fibre remedy? Please provide evidence to support your views.

Question 12.2: Do you agree with our proposed scope of the remedy? Please provide evidence to support your views. Please provide evidence to support your views.

Question 12.3: What scope do you expect to have for cost savings as a result of the proposed dark fibre remedy? How large do you expect any cost savings to be? Please provide evidence to support your views.

Question 12.4: How many orders for dark fibre would you envisage placing during the two-year review period? Please provide evidence to support your views.

Question 12.5: Do you agree with our proposed timeline for dark fibre implementation? Please provide evidence to support your views.

Overall view on dark fibre

Virgin Media does not agree with Ofcom's proposal to implement a dark fibre remedy at this stage. Ofcom has stated that it places a lot of weight on the impact on investment in line with its strategy to promote network based competition. Further, Ofcom confirms that, in this review, dark fibre is only appropriate where material rival investment is *very* unlikely (emphasis added)[15]. Further,

[15] Consultation paragraph 12.77

remedies should be targeted upstream, so that infrastructure rather than service based competition can be incentivised.

Ofcom is proposing a significant change to its regulation of passive access, through the introduction of an unrestricted DPA remedy for the first time in the business connectivity markets. This is a significant step, and as Ofcom rightly points out, one for which it will take some time to establish the new competitive levels once it begins to be taken up. There is considerable interest in the new DPA remedy across industry, and there has been significant interest already in the revised DPA remedy introduced through the Wholesale Local Access market review.

It is important to understand the context of this review. The intent of Ofcom, as set out in the introduction to this review, is to align the access reviews (WLA and BCMR) at the point current WLA regulation is due to end (2021). This review therefore bridges the gap to that end point, and is in that regard an interim review. It is also of note that the timings of this review and the opportunity for consultation and comment are significantly less than they have been for previous 'full' BCMR reviews.

Ofcom specifically acknowledges this in its leased line charge control review. Ofcom notes that the review period covers "a relatively short period" as "we transition to the introduction of new, long term downstream regulation"[16]

In that context, and in light of uncertainty about the impact of DPA on the competitive landscape of business markets, it is inappropriate to impose a new "downstream" passive remedy in the form of dark fibre access alongside DPA. This risks a new (and potentially competition inhibiting) remedy being introduced when a full review for the combined access market is likely to start later this year (and which will be far better equipped to consider market dynamics over the next forward looking period).

The risk to introducing dark fibre in an area that may become competitive (or move towards competition) is clear. Ofcom proposes to price dark fibre on an at cost basis. In simple terms, this removes any incentive for a provider to build rather than buy, and Openreach's position as the monopoly provider in that market will be entrenched.

Given the consequences of an erroneous imposition of dark fibre, the bar must be set very high. It is vital that such a remedy should only be imposed when there is a clear view of where the areas are with no prospect for competition and where that hypothesis has been tested rigorously: at this stage it is simply not clear enough where these areas may be. Further, there is no need to rush through a new service when the new regulation for 2021, only two years ahead, will be proposed later this year, and a much more strategic and coherent approach can be taken.

The counter argument would be that later introduction of a remedy will delay any real benefits that may be brought by that remedy. However, if the introduction of dark fibre is not able to be achieved

[16] LLCC Consultation paragraph 1.3

within one month of the statement, as proposed, any time benefits of early regulation are further reduced. We discuss our views on the proposed timings below.

Ofcom accepts that dark fibre should only be introduced to the extent that competition cannot be brought to an area or market by DPA. Although Ofcom asserts that DPA is unsuitable to provide inter-exchange connectivity, there appears to be little argument to substantiate this. It is of note that all of the advantages cited by Ofcom for dark fibre at paragraph 12.5 (et seq) of the consultation would also be available under DPA.

Ofcom accepts that even aside from DPA, there are other solutions for inter-exchange connectivity available today. In particular, OSA Filter Connect allows for customers to scale bandwidth to need, and allows a lot of the flexibility of dark fibre whilst retaining a degree of management. Ofcom notes that there is less certainty “that a provider would use dark fibre instead of an OSA service purely on the basis of cost savings”[17]. This undermines one of the key dark fibre benefits suggested by Ofcom, that costs savings will incentivise dark fibre take up. If there are already sufficient active products available to the market, then there is no need to introduce a new dark fibre remedy, especially in light of DPA being available, certainly within this transitional review, when the consequence of doing so could disrupt and stagnate potentially more competitive areas.

View on Ofcom’s dark fibre proposals

Notwithstanding our view that dark fibre should not be introduced under this review, we have also considered Ofcom’s proposals in relation to how dark fibre should be implemented.

We agree with Ofcom that it would be inappropriate to mandate dark fibre from any BT+1 exchange, and agree that the imposition of such a remedy would deter future investment. In addition, it would undermine current investments made to co-locate at (or adjacent to) an exchange in order to provide backhaul services, and this would send the wrong message to network investing industry participants who could view this as an indicator of further policy shifts in future.

Ofcom proposes to limit dark fibre availability to BT+0 exchanges. As discussed above, we do not consider that the group of exchanges in the BT+0 category reflects sufficiently those exchanges that are candidates for competition. We have identified [✂] exchanges from which we could offer competitive backhaul services and to which it would be economic to extend our network [✂]. These exchanges should be moved to the BT+1 market. To this end we also think that Ofcom should consider where other providers could also viably reach an exchange to offer backhaul services. Such exchanges should also be excluded from the BT Only market. For example, we note that Ofcom acknowledges that two “BT Only” exchanges are in BT+2 access areas (where regulation is deliberately light touch due to the increased competitive conditions in the area, through network availability). Such exchanges should also be moved to at least the BT+1 market given that there is prospect for backhaul competition in these areas. It would be counterintuitive to allow a CP to purchase dark fibre for one use, but not benefit from charge controlled EAD for another.

[17] Consultation paragraph 12.61

We understand that Ofcom considers the design of the dark fibre remedy to be similar to the design of the remedy for DFA under the 2016 review. This has led to the proposal for an implementation period of only one month following the final statement. Virgin Media considers this implementation period to be too short. The proposed dark fibre remedy is for a specific use case, inter-exchange connectivity, that has not been previously considered, either by Openreach, or the wider industry as potential purchasers of the service. Virgin Media considers that the proposed dark fibre obligation is likely to require a different form of commercial product than the previous DFA product developed as a result of the 2016 market review. Whilst a requirement to supply dark fibre, as a simple fibre connection between two points, may not differ in terms of the imposing regulation (ignoring restrictions on inter-exchange use only and pricing differences between 2016 and this proposal), it is the Reference Offer that will set the commercial terms under which dark fibre will be supplied. On past experience (including the negotiation of the previous dark fibre reference offer), one month is simply unrealistic to develop and agree a suitable commercial proposition for a new product.

In this context, it is also significant that dark fibre has been a controversial remedy over recent years. This, in our view, provides further justification for considering it instead in the broader, holistic review of the access markets that Ofcom plans to undertake later this year. DFA was the subject of the 2016 appeal, although as the underlying market analysis was overturned, any consideration of the remedy was not required by the CAT, and its implementation is at the very least an extremely sensitive subject. It is significant that the implementation period for dark fibre of one month post statement is even shorter than the two month period allowed to lodge appeals from any decision taken by Ofcom.

Ofcom has also already had to clarify the extent of the proposed remedy to confirm that it is an inter-exchange remedy only (rather than providing a more generic dark fibre circuit from an exchange). We consider that the clarification was necessary as any decision to introduce dark fibre has to be on a very tightly controlled basis given the potential risk to competition. However, that there has already been confusion as to the scope of the remedy means that the Reference Offer process becomes more important than ever, and as stated above, this is not something that should be required to be completed within a single month.

Virgin Media is also concerned that dark fibre could be used more widely than anticipated by Ofcom. The rationale for Ofcom to propose dark fibre in this context is to provide better connectivity from a BT exchange location where there is no alternative provider of connectivity. That circuit should only do what is necessary to alleviate the absence of competition. Therefore, it should allow connectivity to the next exchange where backhaul competition can be provided. It should not be used to act as pseudo-trunk connectivity to carry traffic long distances in order to avoid backhaul charges.

Dark fibre pricing

Ofcom has changed its pricing proposals from the DFA product in the 2016 review (which was active minus based on a 1Gb EAD price), by proposing a cost based, per km charge for dark fibre.

This is significant in the context of the cost of the circuit, and could substantially reduce the price of the dark fibre circuit (depending on length). We understand Ofcom's rationale in that the remedy proposed here is far more targeted at a market that Ofcom believes is uncompetitive and unlikely to become competitive in the future. In those terms, there should be less risk to investment as Ofcom has proposed that the areas in which the remedy will be available would be those that would not attract investment in any event. Whilst that is sound in principle, it means that there is an additional responsibility on Ofcom to ensure that the remedy does only apply in areas that are truly uncompetitive AND that such conditions are enduring. We have set out above our concerns in relation to the availability of the remedy, and the proposal for cost base pricing only serves to highlight those concerns.

Virgin Media agrees with Ofcom that there would not be any material cost savings resulting from the provision and maintenance of two fibres over a single fibre[18], and therefore the cost based charges for a two fibre service should be twice those of a single fibre variant.

Specific remedies for active products

Question 13.1: Do you agree with the specific network access remedies that we propose for CI services at all bandwidths in the business connectivity markets? Please provide evidence to support your views.

Virgin Media broadly agrees with the proposed specific CI network access remedies described by Ofcom in Section 13 of the consultation. We agree that it is appropriate to apply different remedies to the different areas within the CI access market and support Ofcom's treatment of HNR areas, reflecting that these are areas where competition is emerging[19], by not imposing a specific price control in these areas.

We also agree that the price controls applied outside of HNR areas should ensure that efficient investment is promoted and that, in this transitional period flat pricing is the appropriate remedy for these services[20].

We disagree with Ofcom's proposals in relation to dark fibre inter-exchange circuits for the reasons set out above, and consider that the proposed specific access remedies are sufficient to address the identified completion concerns in these markets, taking account of and complementing the proposals for unrestricted duct and pole access.

[18] LLCC Consultation paragraph 4.16 noting two exceptions to this rule, one-off connection and cessation, with which Virgin Media agrees.
[19] Consultation paragraph 13.6
[20] Consultation paragraphs 13.43 and 13.44

Specific remedies for interconnection and accommodation

Question 14.1: Do you agree with the specific remedies for interconnection and accommodation that we propose? Please provide evidence to support your views.

Virgin Media also agrees with Ofcom's proposals for interconnection and accommodation remedies as described in Section 14 of the consultation; these services are necessary to support the provision of regulated connectivity services in areas where BT is dominant, and therefore, it is appropriate that they continue to be regulated. Such services are equally important as the connectivity services they support, and where they are a required part of an overall solution, they need to be regulated, as proposed, to ensure that the supply of an ancillary service does not impede the delivery of the overall solution.

Quality of services (QoS) remedies

Question 15.1: Do you agree with our proposals regarding the application of QoS standards, KPIs, SLAs and SLGs over the period of this review? Please provide evidence to support your views.

Virgin Media has no comment on QoS proposals.

Remedies in the Hull Area

Question 16.1: Do you agree with the remedies in the Hull Area that we propose? Please provide evidence to support your views.

Virgin Media has no comment in relation to regulation of the Hull Area

Volume 2: Leased line charge control

Objectives and approach in setting the leased lines charge controls

Question 2.1: Do you agree with the proposed form of charge controls? Please provide evidence to support your views.

Virgin Media supports Ofcom's approach to setting charge controls and agrees that a key objective should be to promote certainty for network investors.

Ofcom's decision to apply a CPI-CPI control, rather than a CPI-X control allows for stable pricing during the period prior to the new joined approach to the access market review in 2021. Virgin Media agrees with Ofcom's proposal that pricing stability is more important in the overall context of this review than the need to impose strict cost based controls, recognising the importance of pricing certainty and stability and creating the right conditions to promote certainty for investment in networks to bring competition to the market[21]. Further, we note that the potential gap between cost and the proposed approach is relatively small (within £50-65m), resulting in minimal loss of short term consumer benefit associated with an FAC based control.

The proposed approach is does not simply reflect a decision to apply a safeguard cap, but takes account of cost modelling in order to ensure that the approach can satisfy the relevant tests under the Communications Act.[22]

We also agree with Ofcom's approach to the VHB market. This is a more competitive area of service and there is a competitive control to BT's pricing in any event (illustrated by downward trends in VHB pricing). This effect will be further reinforced by the introduction of services based on the new DPA remedy. The proposed safeguard cap ensures that Ofcom is maintaining a backstop regulatory control over pricing. We do not consider that it would be proportionate to impose a more intrusive remedy over these services, especially having regard to Ofcom's overall intent to ensure pricing stability for investors.

It is important to have regard to the timing of this review period. The review is acknowledged by Ofcom as applying to a short period and a transition before the new unified approach to business and residential access markets is taken from 2021. That this review's purpose is to bridge a gap further reinforces the proposal to ensure that stability is prioritised on this occasion.

We have set out our position in relation to dark fibre pricing above, but Virgin Media remains concerned that the adoption of strict cost-based pricing would mean that the risk that potentially

[21] LLCC Consultation Paragraphs 2.4 to 2.6
[22] Including section 88 of the Act

competitive areas are inadvertently regulated carries higher consequences: cost based pricing will certainly eliminate any prospect of competition from these areas.

Charge control design

Question 3.1: Do you agree with each of our proposals in relation to the design of charge controls for active services at 1 Gbit/s and below? Please provide evidence to support your views.

Question 3.2: Do you agree with each of our proposals in relation to the design of charge controls for active VHB services? Please provide evidence to support your views.

Question 3.3: Do you agree with each of our proposals in relation to the design of charge controls for accommodation services, Excess Construction Charges and Time Related Charges? Please provide evidence to support your views.

Virgin Media considers Ofcom's proposals for charge control design to be appropriate. There need to be separate baskets for 1Gb and below services and VHB services given the different nature of the proposed controls. We also consider that the use of sub-caps as proposed is appropriate. Although this constrains some pricing freedom by Openreach, certain services need to be controlled within the basket. An example of this is Cablelink, which is purchased to facilitate Virgin Media's and other providers' on-net connectivity with purchasing CPs who are located within a BT local exchange. If this is not part of the basket, BT could act to disincentivise connectivity utilising Cablelink products.

Inter-exchange dark fibre charge control

Question 4.1: Do you agree with our proposals in relation to the design of a charge control for inter-exchange dark fibre? Please provide evidence to support your views.

We have set out our views on Ofcom's proposed dark fibre, including the risks of adopting a cost based charge control above.

Implementation, compliance and legal tests

Question 5.1: Do you agree with each of our proposals in relation to the implementation of charge controls? Please provide evidence to support your views.

Virgin Media has no comment in relation to the proposed implementation approach to the charge controls as set out in Section 5, however, this is subject to our comments on the appropriate implementation date for dark fibre (if the proposal to apply dark fibre is confirmed).

Virgin Media
18 February 2019