

Response to Ofcom's consultation

Promoting investment and competition in fibre networks: Initial Proposal – approach to remedies

Joint submission by Colt, TalkTalk, Sky and Vodafone (the 'Passive Access Group')



Submitted to Ofcom: June 2019

Introduction

1. The Passive Access Group or PAG (TalkTalk, Vodafone, Colt and Sky) write in response to Ofcom's consultation on '*Promoting competition and investment in fibre networks – Initial proposals – Approach to remedies*' published on 29 March 2019 (the 'Remedies consultation').
2. The PAG welcomes the opportunity to respond to this consultation. This response is limited to issues that directly and indirectly impact on the PAG's ability to gain access to BT's passive network. This access is important for the PAG as it enables its members to better meet the supply constraints they face by being forced to continue to purchase Openreach's leased lines and other access products.
3. This submission is supplementary to any responses that PAG members provide individually to Ofcom. In the event of any conflict between this submission and any individual responses, this shall be interpreted as the individual responses taking precedence.
4. In this submission the PAG identifies some areas for concern in relation to Ofcom's proposals and seeks to encourage Ofcom to re-consider its approach.

Background to the PAG's position in this consultation

5. The PAG remains of the view, as set out in our response to the approach to geographic market consultation,¹ that it is difficult for stakeholders to provide a fully constructive response to Ofcom's proposed approach to remedies given that Ofcom has not yet carried out a product market analysis.²
6. Similarly, the PAG is concerned with Ofcom's approach to defining the geographic market, making it very difficult to provide a constructive view on the remedies.³
7. In particular, the PAG is disappointed with Ofcom's approach to 'competitive areas' and its decision to deregulate these areas completely⁴ despite the lack of upfront agreement on what effective competition looks like. While the PAG would support Ofcom's proposal to remove regulation where there is sustainable effective competition, this is not what Ofcom is proposing to do. Ofcom's proposal to label as 'competitive' areas where BT plus other two providers are present is unlikely to constitute 'effective competition' in all cases.⁵ It is very likely that BT will continue to have SMP in certain pockets of these areas since Ofcom is proposing to use a threshold of 65% of premises passed⁶ in order to conclude a network is 'present' in a post code sector. This means that many premises

¹ 11 December 2018 "Promoting investment and competition in fibre networks - Approach to geographic markets" Consultation

(https://www.ofcom.org.uk/data/assets/pdf_file/0005/130001/Consultation-Promoting-investment-and-competition-in-fibre-networks.pdf).

² See section 3 to the PAG response to the 'Promoting investment and competition in fibre networks: approach to geographic markets.

³ See section 4 of the PAG response to the Geographic Markets Consultation (Op. cite footnote 2).

⁴ Para 1.11 of the consultation document.

⁵ Para 2.18 of the Approach to geographic Markets consultation (Op. cite footnote 1).

⁶ Para 3.21 to 3.25 of the Approach to geographic Markets consultation (Op. cite footnote 1).

may have no or only one competitor to BT and will still be labelled as competitive. Removing all regulation in these areas, when BT is still able to set prices unconstrained by its competitors will have a damaging effect on the market.

Remedies in the 'potentially competitive' areas: Flat pricing for leased lines

8. The PAG welcomes Ofcom's decision to continue to require BT to provide network access in those potentially competitive areas where BT has SMP, in particular, in relation to MPF and VULA (across all bandwidths).⁷
9. However, the PAG considers Ofcom is wrong in proposing a flat CPI+0% inflation adjusted charge control for all leased lines (i.e. across all bandwidths), and in particular at 1Gbit/s and above, given these bandwidths are expected to see rapid growth and potentially become the largest market segments.⁸ This approach appears to go against the basic premise of cost-based pricing: that higher volumes leads to lower costs (to BT) and will result in super profits, excessive retail prices and weakened competition. The only justification to weaken regulation in these instances is that there is a material constraint on BT in these areas. However, no such constraint exists today and even if an additional alnet FTTP network is rolled out, this is unlikely to deliver a material constraint. There is no evidence to suggest that FTTP networks will address the leased lines market at scale. By way of evidence in the CLA there are, on average, 4.3 network competitors to BT, yet BT has a market share over 61% (and a presumption of SMP).
10. Therefore, flat leased line pricing will result in super-profits for the BT Group, excessive retail prices or scope for a retail margin squeeze by the BT Group. This is particularly concerning as Ofcom intends to introduce these prices while it plans to extend the charge control period to 5 years, thereby extending the negative impact of flat, inappropriately high prices across leased lines and passives.
11. Ofcom's proposal to keep flat prices for leased lines is also made worse by the fact that Ofcom is deciding not to introduce a parallel remedy for BT's prices to be fair and reasonable in those markets where BT has SMP.⁹ A fair and reasonable pricing obligation alongside a charge control can act as a last resort safety mechanism against BT in areas where BT is still dominant; particularly, as a flat price control is likely to give BT too much pricing flexibility (irrespective of other competitive constraints). It is unclear why Ofcom has decided to view this remedy as an alternative and not a supplement to the charge control.
12. For these reasons, one option to address rapidly changing competitive conditions is for Ofcom to carry out a mid-market review assessment given market review periods are being extended to 5 years. Ofcom should seek to determine whether the remedies applied to each area are still appropriate half-way through the market review period. This is particularly so given Ofcom's decision to carry over the charge controls from the current market review period by only adjusting for inflation.

⁷ Para 2.11 of the consultation document.

⁸ Para 2.32 of the consultation document.

⁹ Para 2.29 of the consultation document.

Ofcom's approach to addressing BT's market power in the CLA

13. The PAG disagrees with the conclusions, which are unsupported by the evidence, made in the draft BCMR statement concerning SMP in the CLA. The PAG raised several points in relation to a 'no SMP finding' in the CLA area in their BCMR and PIMR consultation responses that Ofcom has failed to address, in particular:¹⁰
 - a. The fact that BT have a market share in the CLA area of over 61%, which is sufficient to engage a presumption of dominance. Ofcom has not demonstrated that the presumption of dominance has been rebutted in order for it to find no SMP.
 - b. Similarly, Ofcom has not considered additional factors that further support a finding that BT has SMP in the CLA, such as particular supply characteristics in the CLA geographic area.
14. Ofcom's proposals to not impose regulation in areas which are effectively competitive has the effect of deregulating the CLA area even though BT has a 61% market share, yet Ofcom have not provided enough evidence to rebut the presumption of dominance. The PAG considers this approach will hinder effective competition in the CLA area and harm consumers. Therefore, the PAG encourages Ofcom to conduct further analysis and asks it to reconsider its current proposals for remedies in the CLA area.

Dark fibre as a remedy only available in non-competitive areas

15. The PAG supports the imposition of dark fibre access ('DFA') on a cost basis in non-competitive areas.
16. However, the PAG disagrees with Ofcom's approach to limit the use of DFA to 'non-competitive areas' only.¹¹ It is not clear to the PAG what analysis Ofcom has carried out to conclude that DFA will materially affect OCPs' incentive to invest in networks. Equally concerning is Ofcom's assumption that that the benefits of a small increase in network investment will be greater than the benefit cost-based DFA will deliver to the market as the active layer is opened to competition. DFA is likely to deliver significant innovation and efficiency to many customers.
17. It also appears to us that Ofcom has not taken into account the value for end-users of OCPs having both unrestricted Duct and Pole Access ('DPA') and DFA available at a regulated price (it will mean much more choice for consumers both in the short and long term). In this sense Ofcom is (once again) deciding, without appropriate basis, to limit the toolkit available to market participants to pursue efficient supply of their choice and

¹⁰Ofcom does not address the problems which have been raised by the PAG in its BCMR, PIMR and approach to geographic market consultation responses. See paragraph 10 of the PAG 2019 BCMR consultation response; paragraphs 6 to 11 of the PAG's PIMR consultation response.

¹¹ See PAG PIMR response paragraphs 12 – 13; PAG BCMR response paragraphs 12 – 17 and PAG 'Approach to Geographic Market Consultation response at paragraph 4.4.

therefore artificially constraining the scope of competition that could emerge without these constraints. There is no legal or economic reason for taking this decision.

18. Ofcom's approach is based on the untested assumption that Other Communication Providers ('OCPs') will find it more commercially attractive to use DFA than DPA. However, if/when both DPA and DFA are/were available, some OCPs may prefer to use DFA given it provides most of the benefits of DPA at acceptable cost levels without the barriers to roll out. Ofcom should focus more on facilitating greater choice of potential remedies for OCPs, which will promote more competition with BT and between OCPs.
19. As DFA is an extremely useful remedy to address mobile and fixed network capacity constraints, the PAG is also concerned that limiting DFA to non-competitive areas does not go far enough to address the UK's growth in demand for fixed access bandwidth and the requirements of 4G and 5G networks. This concern is amplified by Ofcom proposals to introduce the remedy only in non-competitive areas which, following Ofcom's position in the geographic markets consultation, is likely to amount to a very small portion of the national territory (basically rural areas).
20. The PAG urges Ofcom to re-consider its proposal to limit the DFA remedy to non-competitive areas.

Conclusion

21. Demand for higher bandwidth services is growing exponentially, and remedies such as DFA are crucial to meet this increase in demand and enable the successful implementation of new technologies which will contribute to the overall benefit of consumers and the UK economy. Ofcom's approach may mean that OCPs cannot meet the demand of consumers by refusing to impose DFA in areas which will give OCPs the best chance of competing effectively with BT. Instead, Ofcom's approach appears more focused on ensuring BT has adequate return on investment by keeping prices flat.
22. Ofcom has failed to justify its approach in the truncated 2019 BCMR and are now proposing to build on these errors in this consultation. The PAG emphasises the points it made in its BCMR, PIMR and the geographic market consultation responses. It requests that Ofcom review its approach and take the PAG's comments into account.