Response to the
Consultation on Non-domestic rates and the price of regulated Dark Fibre

by the
Infrastructure Investors Group

Report Produced by GOS Consulting Limited

Contents

1 Introduction and Summary

1.1.1 The IIG is pleased to set out in this document its comments on Ofcom's consultation on non-domestic rates and the pricing for regulated Dark Fibre (The NDR consultation).

1.1.2 The IIG considers that Ofcom's proposals in the NDR consultation are likely to have a number of negative effects on the markets for electronic communications networks and services in the UK, the level of competition and investment, and potentially cause competition distortion in a number of markets, including:

- Increasing the negative impact of the LLCC and DFA pricing on infrastructure investment in the UK,
- Creating winners and losers in the market, and
- Causing competitive distortions in downstream markets

1.1.3 The IIG further considers that Ofcom's proposals are over-simplified, not taking into account the full scope of the CMA decision and not based on sufficient transparent analysis to provide confidence that their consequences are fully understood by Ofcom.

1.1.4 With regards to Ofcom taking into account the full scope of the CMA's Final Determination (FD), the CMA stated the following (FD Paragraphs 3.251 – 252, emphasis added):

"[]CityFibre said that, in relation to the TalkTalk appeal, the CMA's provisional determination is relevant to the effect of the BCMR on CityFibre and on infrastructure competition generally. CityFibre said that the CMA should take this impact on infrastructure competition into account in its decision concerning CityFibre's case.

This is not the reference question which we were asked by the CAT in respect of the CityFibre appeal. As discussed in section 6, we will give guidance to the CAT that the pricing of DFA should be considered further by Ofcom, and we would expect that Ofcom's considerations would be made in light of all the relevant circumstances."

1.1.5 The IIG calls on Ofcom to withdraw the current consultation and replace it with one that reflects the full scope of the FD and ensuring that any proposals are fact-based with sufficient and transparent analysis presented for Communications Providers

2 The Infrastructure Investors Group

2.1.1 The Infrastructure Investors Group (The IIG) is a collective of alternative infrastructure providers who have built, own and operate high-speed electronic communications networks within the UK, independently of BT. Whilst the members of the IIG normally compete intensely with each other, they believe that it is important to present a strong voice to protect a pro-investment environment for electronic communications networks in the UK and have come together for this sole purpose.

2.1.2 The members of the IIG are (in alphabetical order):

- CityFibre Infrastructure Holdings plc

- euNetworks Group Limited
- Virgin Media plc
- Zayo Group LLC

2.2 CityFibre Holdings

2.2.1 CityFibre is the UK's largest alternative provider of wholesale fibre network infrastructure. It has major metro footprints in 42 cities across the UK and a national long distance network that connects these cities to major data-centres across the UK and to key peering points in London. The company has an extensive customer base spanning service integrators, enterprise and consumer service providers and mobile operators. CityFibre provides a portfolio of active and dark fibre services, CityFibre's networks. As at 31 December 2016, CityFibre operated 2,244 kilometres of metro local access duct and fibre networks across 42 towns and cities, as well as a 1,139 kilometres national long distance network connecting 22 towns and cities to data centres in London and the UK regions. CityFibre is based in London, United Kingdom, and its shares trade on the AIM Market of the London Stock Exchange (AIM: CFHL).

2.3 euNetworks

2.3.1 euNetworks is a European provider of bandwidth infrastructure services. It owns and operates 14 fibre based metropolitan city networks in 5 countries, connected with a high capacity intercity backbone covering 48 cities in 13 countries. euNetworks leads the market in data centre and cloud connectivity provider in Europe, directly connecting over 300 data centres in Europe, with further data centres indirectly connected. euNetworks was founded in 2002 and has its headquarters in London.

2.4 Virgin Media

2.4.1 Virgin Media is the second largest provider of broadband infrastructure within the UK. Its network – the result of multi-billion pound private investment – delivers ultrafast broadband with speeds of up to 350Mbps, as well as market leading connectivity to thousands of public and private sector organisations. Virgin Media is a part of Liberty Global plc, the world's largest international cable company, together serving 24 million customers across 14 countries.

2.5 Zayo Group

Zayo Group is a global provider of communications infrastructure services, including dark fibre, wavelength, Ethernet and IP services. Zayo operates in the United States, Canada, France, Germany, Netherlands, Belgium, Switzerland, Italy, Ireland, and the United Kingdom. Its UK fibre optic network spans more than 450,000km and connects over 130 data centres via unique routes alongside the national gas pipeline and within London's sewer system. Zayo was founded in 2007 and is headquartered in Boulder, Colorado, with European headquarters in London and Paris.

2.5.1

3 How Ofcom's proposals will impact the market and different types of communications providers (CPs)

3.1 The DFA price resulting from Ofcom's NDR adjustment will increase the negative impact on investment incentives

3.1.1 Having reviewed the CMAs Final Determination (FD) and Ofcom's NDR consultation[1], the IIG is disappointed to find that, despite the accepted positon that the introduction of DFA will have negative effects on investment incentives, Ofcom is proposing a further and significant reduction of the DFA price

3.1.2 Although Ofcom considers that there will be no significant incremental impact on investment incentives[2], the IIG considers is evident that such a significant price reduction of the DFA remedy will have a negative impact on the ability of CPs to invest in new networks and offer dark fibre products in competition with BT.

3.1.3 Ofcom recognised in the BCMR that there would be negative impacts on investment incentives; this concern is repeated in the NDR consultation. The justification of such a remedy was that other benefits outweighed the negative impact on investment incentives. Given the importance placed on network built and investment incentives in the DCR, any decision that negatively affects these incentives must not be taken lightly.

3.1.4 The approach of Ofcom to propose a simplistic reduction of approximately £200 per annum in the DFA price, as fully addressing the CMA's concerns, creates a situation where as a matter of simple logic a cheaper product will be more attractive to purchase, and therefore, the negative impact on investment incentives will be increased. Although Ofcom argue that the adjustment simply brings pricing into line with their original intent of creating a "cost neutral" purchasing decision between an active 1Gb product and dark fibre, the change is nevertheless a significant reduction on the DFA pricing compared to that determined in the BCMR.

3.1.5 In this context, it is important to recall that Ofcom, in the BCMR, considered that the (then) proposed price level for DFA struck the right balance between generating sufficient demand for DFA, without significantly damaging efficient investment[3]. A significant reduction in price from that level should warrant a transparent analysis of its impact. As stated above, the FD specified that Ofcom should take into account all relevant circumstances, which included the impact on infrastructure competition in reviewing the pricing methodology for the DFA remedy[4].

3.1.6

[1] Which the IIG understands is intended to implement the CMA's FD in its entirety.
[2] FD Paragraph 1.13 (a)
[3] BCMR Final Statement paragraph A20.18.
[4] FD Paragraphs 3.251-3.252.

3.2 Ofcom has oversimplified the NDR consultation to ensure that the DFA remedy launch is not delayed

3.2.1 Ofcom has requested no data from CPs and has undertaken no transparent analysis to show that its proposed change to the value of the NDR element in the DFA pricing formula will satisfy the concerns and failings set out in the CMA's Determination.

3.2.2 Ofcom's assumptions of CPs' existing contiguous networks, average circuits length, etc. are, to the knowledge of the IIG members, not based on information requested by CPs, but rather on the EAD circuits currently contracted from BT Openreach which would give no indication of how the different circuit lengths are distributed between different CPs or classes of CPs.

3.2.3 There are numerous references throughout the consultation to assumptions and beliefs used to justify an approach without any appropriate levels of analysis or scrutiny.

3.2.4 Although Ofcom justifies this approach with an intent to only make adjustments that are "simple and practical"[5], this is insufficient, especially in light of the CMA's specific requirement for Ofcom to "determine an amended DFA pricing methodology in accordance with its regulatory objectives"[6]

3.2.5 The IIG considers that Ofcom has not developed its proposed changes to the DFA pricing in accordance with it regulatory objectives and that it is not possible for Ofcom to know the impact of its proposals, given that it has not requested any data from CPs to enable it to do so.

3.3 Ofcom's proposals are discriminatory

3.3.1 Ofcom cannot safely assume that its DFA pricing proposal will have a competitively neutral impact on the many different types and sizes of CPs who could purchase DFA and incorporate the DFA remedy into the services they provide to different types end users. The size of contiguous networks operated by CPs in the UK varies considerably, as does the type and length of circuits used.

3.3.2 Ofcom assumes that CPs that today use active leased lines would be able to easily convert these to DFA circuits (which would then qualify as a contiguous network according to the VOA's tone table). This assumption is made without taking into account the costs and time required to make such changes, and the likely disruption to end customer's services which would be a significant barrier to any CP undertaking such a mass conversion of circuits.

3.3.3 If Ofcom's proposals are implemented, the IIG has identified four distinct groups of CPs[7] which will be affected differently by those proposals – likely resulting in competitive distortion, and reduced investment:

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[5] NDR Consultation Paragraph 2.13

[6] FD paragraph 6.21 (a).

[7] These are CPs that would use the DFA remedy, if it were economically viable, not competing infrastructure providers.

- Those CPs that do not match Ofcom's representative profile because (e.g. have smaller contiguous networks or longer average circuit length) . For these CPs the DFA remedy is unlikely to be commercially attractive or even viable because as their NDR liabilities would exceed the amount included in the DFA pricing formula. Those CPs are unlikely to use the DFA remedy to any significant extent;

- Those that fit Ofcom's representative profile and may use the DFA remedy as anticipated by Ofcom;

- Those that do not match Ofcom's representative profile because they have large networks with multiple fibres in each duct, and who accordingly face lower NDR costs than assumed by Ofcom. These CPs will consequently be put in an advantageous position compared to the first two groups and will be likely to use the DFA remedy more extensively, cannibalising more active products than anticipated by Ofcom; and

- The three CPs (BT, KCOM and VM) who do not qualify for the NDR reduction. This is due to differences in their exposure to NDRs, but could create distortions where circuits are supplied in the wholesale market to resellers, in which case the exact same circuit would be cheaper from an alternate wholesaler.

3.3.5 This feature is recognised and accepted by Ofcom in the consultation, but summarily dismissed without any appropriate analysis.

3.3.6 Ofcom ought to collect information regarding the existing contiguous networks of CPs, the average and spread of circuits lengths by CP or by group of CPs, in order to understand the impact on the demand of DFA of its proposed pricing change.

4 Summary

4.1.1 The members of the IIG are active investors in infrastructure in the UK. The LLCC and the DFA pricing as set out in the BCMR Final Statement in April 2016 has and is having a chilling effect on investment in competing electronic communications network infrastructure of all types in the UK and the proposals in the NDR consultation will exacerbate that effect.

4.1.2 Ofcom's proposals appear founded on little relevant analysis and no analysis of the likely impact on any groups of CPs has been presented. Ofcom's analysis appears to be limited solely to ensuring that BT is able to recover its relevant costs.

4.1.3 The IIG considers that the proposed new DFA pricing will have wide-ranging consequences across many different parts of the UK electronic communications markets, potentially destabilising competition in some and reducing investment incentives in many, and that it ought to be considered properly before being implemented. Adherence to an arbitrary launch deadline, cannot take precedence over ensuring that the remedy is specified such as to maximise benefits and reduce adverse effects.