

WLA 2017 Team
Ofcom
Riverside House
2a Southwark Bridge Road
London
SE1 9HA

12 January 2018

Cc: [redacted]

NON - CONFIDENTIAL

Response to Wholesale Local Access Market Review – Promoting Network Competition in Superfast and Ultrafast Broadband

Executive Summary

BT Openreach has both incentive and capability to price wholesale access products at levels to undermine investment in alternative 'fibre-to-the-premises' (FTTP) network operators.

As alternative network providers to that of BT Openreach have now secured funding for substantial FTTP network expansion, the threat of such activity is to a level that risks undermining this planned delivery.

As both Ofcom and Government acknowledge the importance of both FTTP rollout and competition at a wholesale access network level¹, Ofcom should act to deny BT Openreach the ability to target areas that cover a planned alternative FTTP network footprint with reduced wholesale pricing.

This would limit BT Openreach's capacity to reduce wholesale prices purely to undermine FTTP roll out in a defined region, as such a reduction would then need to be conducted at a national level, so would consequently incur a larger cost for BT.

Gigaclear then supports Ofcom's proposal of expanding the definition of 'undue discrimination' to include a restriction on such activity.

Within this consultation, Ofcom also discuss the risk of BT deliberately targeting network upgrades to areas where alternative operators are scheduled to deliver FTTP networks.²

Such activity would undermine the business case for roll out in that area, as the upgrading of current BT Openreach lines prior to the alternative network going live would reduce the

¹ https://www.ofcom.org.uk/data/assets/pdf_file/0021/108381/consultation-wla-competition-superfast-ultrafast-broadband.pdf paragraph 2.2

² https://www.ofcom.org.uk/data/assets/pdf_file/0021/108381/consultation-wla-competition-superfast-ultrafast-broadband.pdf paragraph 3.4

expected rate of take up on the alternative network, thereby deterring investment and despoiling the area from build plans.

Yet Ofcom does not offer a remedy to this concern, as the remainder of the consultation discusses how to address the risk of regionally targeted price reductions at a wholesale level.

[§] This risk appears to be highest where BT have failed to secure a BDUK tender and then utilise commercially funded build to undermine the planned build of the competitor that has secured the tender.

To address this issue, we propose that where alternative network operators are successful in securing state aid for delivering new infrastructure, BT Openreach is denied from upgrading its infrastructure within the relevant intervention area for the following three years.

Introduction

As a rural fibre-to-the-premises (FTTP) network operator, Gigaclear delivers full fibre network solutions to areas that have historically received poor download speeds due to the limitations of copper based broadband over long distances. This means that Gigaclear invariably rolls out its network in areas that are solely served by BT Openreach.

Across the period of the WLAMR charge control, multiple alternative operators to BT Openreach will be accelerating the roll out of their FTTP network footprints. Meanwhile BT has consulted the wider industry on providing FTTP to 10 million premises by 2025.³ In the meantime BT continues to deliver and bid for BDUK tenders, within which BT offer VDSL2 upgrades to ADSL technology, along with elements of FTTP.

BT itself acknowledges that both VDSL and (albeit to a lesser extent) FTTP are quicker to rollout and cheaper to deliver (when compared to an alternative operator installing new FTTP infrastructure), where there is pre-existing infrastructure in the ground.

BT Openreach is then capable of using both;

- wholesale access product upgrades to improve download speeds ahead of alternative network providers commencing the roll out of an FTTP network in a known defined area, and;
- regionally targeted wholesale price reductions to increase take up of BT Openreach enabled retail products, thereby decreasing the propensity of customers in the area joining an alternative network.

The threat of the incumbent seeking to protect its position of dominance by undermining competition at the access network level is then very real, with even the prospect of such activity being likely to deter investment, especially when there are clear incentives for such activity.

³ <https://www.openreach.co.uk/org/home/updates/briefings/generalbriefings/generalbriefingsarticles/gen04717.do>

In the following paragraphs, we set out our position on the topics raised within the consultation, as well as offering evidence to justify our recommendation of a three-year freeze on BT Openreach upgrading infrastructure within BDUK intervention areas where the tender is awarded to a competitor network.

Incentive

Ofcom has already established that BT has significant market power within the Wholesale Local Access Market.⁴ , this means that BT enjoys a position equivalent to dominance, that is to say a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers. In economic terms, this is often associated with a demand inelastic product that is provided through a monopolistic market structure.

In such a scenario, the most evident danger is that the incumbent seeks to profit maximise, raising prices and gaining from the absence of an alternative provider and viable alternative services to that of broadband connectivity. Further, with the absence of a viable alternative, these profits risk not being reinvested into the infrastructure to improve service to the extent that they otherwise would be under a competitive environment.

In considering restrictions to be placed upon BT to address its position of SMP, Ofcom is then right to directly consider pricing and quality of service parameters in its analysis of the potential harm to end-users.

Whilst this is clearly commendable, it does not address another logical consequence of SMP; that being the incentive to retain the position of SMP. As stated above, a position of dominance enables BT to accrue profits beyond what would be achievable in a competitive market.

Without regulatory intervention, BT is then incentivised to undermine the development of alternative networks. This could be done in multiple ways, one of which would be to cross subsidise wholesale services in target areas that cover a planned alternative FTTP network footprint with reduced wholesale pricing. The reduced pricing would increase take-up of BT (and partner) services at a retail level and consequently undermine the expected uptake of the planned alternative network; therefore, deterring planned build and undermining investor confidence more broadly through the fear that such activity could occur elsewhere.

Short term targeted price reductions could then be worthwhile for BT, as the short-term impact upon revenues is worth securing a position of dominance.

Such an outcome would then undermine Ofcom's stated ambition of enabling three fibre networks in over 40% of the UK.

This danger is not a new phenomenon; in wholesale end-to-end voice telephony, BT has historically pursued aggressive targeted pricing that sought to deter competition and

⁴ https://www.ofcom.org.uk/data/assets/pdf_file/0021/108381/consultation-wla-competition-superfast-ultrafast-broadband.pdf paragraph 1.1

increase market share. Following Ofcom's investigation into this activity, Ofcom itself confirmed that margin squeeze had occurred,⁵ thereby gaining market share.⁵

The harm is then counter-intuitively derived from reduced (as opposed to increased) retail price levels. Whilst there may be a 'short-term' gain for consumers in the sense that retail prices are reduced, the price reduction is ultimately for the strategic purposes of a SMP wholesale provider seeking to utilise its incumbency to stifle future network level competition. It would then be short sighted to claim that such price reductions are in any way to the genuine benefit of the consumer. Further, should such activity prove successful in deterring the development of alternative networks, BT would once again be incentivised to increase prices. Consumers then lose the short term benefit of lower retail prices, as well as the opportunity to be offered an alternative network operator in the future.

Capability

As the national incumbent, BT Openreach has a significant logistical advantage over alternative network operators in that it already has substantial infrastructure on (or rather in) the ground. It then has a pre-existing presence where alternative networks plan to rollout FTTP.

On top of this, as BT Openreach state within their own consultation documentation, the timeframe for upgrading ADSL to VDSL2 and VDSL2 to G.fast is significantly shorter to that of having to install new infrastructure. Further, recent trials suggest that BT Openreach can utilise pre-existing infrastructure to accelerate the delivery of FTTP.⁶ BT Openreach can then choose to upgrade services to improve download speeds more quickly than an alternative network operator can deliver new infrastructure to the same area.

This risk is exacerbated where planned rollout is supported by state aid. Under the national broadband scheme, broadband delivery supported by state aid must designate properties to receive the new service within the initial Invitation to Tender. Whilst this is done to inform applicants when analysing and designing a potential bid, it also functions to broadly disclose where the successful applicant will be rolling out the new network.

In scenarios where BT bids for such support (most commonly under the BDUK process) but is then unsuccessful, it is then aware of where the successful applicant will plan to roll out its network to a considerable level of accuracy. Whilst BT (if unsuccessful) cannot then leverage other forms of state aid to deliver services within the designated intervention area, it can still choose to upgrade pre-existing services in this area on its own commercial basis. As BDUK intervention areas are designated for their low (less than 30mbps) access line speeds, upgrades prior to the arrival of the new network infrastructure can dramatically alter the propensity of potential customers leaving the incumbent and moving to an alternative network. BDUK bids can then function as a signal for the incumbent to prioritise a location for commercial upgrade – thereby enhancing its capability to strategically undermine alternative FTTP network rollout. Alternatively, BT can then leverage its

⁵ https://www.ofcom.org.uk/data/assets/pdf_file/0018/79011/final.pdf

⁶ <http://www.eastmidlandsbusinesslink.co.uk/mag/news/east-midlands-firms-promised-uks-fastest-broadband/>

community fibre partnership programme⁷ to prioritise roll out in the area where the alternative network is commencing build.

[✂]

- [✂]
- [✂]
- [✂]

Associated Risks

As described above, BT has both incentive and capability to strategically undermine investment in and rollout of alternative FTTP networks. This can then largely manifest itself in two ways:

- regionally targeted wholesale price reductions to increase take up of BT Openreach enabled retail products, thereby decreasing the propensity of customers in the area joining an alternative network.
- wholesale access product upgrades to improve download speeds ahead of alternative network providers commencing the roll out of an FTTP network in a known defined area.

Regionally Targeted Wholesale Price Reductions

To address the first point, Gigaclear supports Ofcom's proposal of expanding the definition of 'undue discrimination' to effectively include an ex-ante national pricing obligation. This will deny BT the ability to target wholesale price reductions at regions where alternative FTTP networks are planning to rollout a fibre network. Such a solution is simple to implement and places no onerous requirements upon any network operator in order to be enforced.

We acknowledge that Ofcom is historically hesitant to implement ex-ante regulation,⁸ and is more comfortable in prescribing regulatory intervention when demonstrable need is evident and harm is already present. However, under the Communications Act, Ofcom is obliged to promote competition in the provision of telecommunications networks and services. To rely wholly on ex-post regulation to do this would in effect permit the incumbent to act to undermine competition until evidence of such harm was evident and had been analysed to confirm a causal link to the incumbent's activity.

⁷ <https://communityfibre.openreach.co.uk/>

⁸ As expressed in Ofcom's removal of the Wholesale Must Offer Obligation for Sky's premier league content.

Such an approach could have a substantially detrimental impact upon current investment in FTTP networks. CityFibre and Hyperoptic have both announced plans to substantially increase their network footprint during the WLAMR charge control period. Virgin Media has also publicly committed to continuing its Project Lightning rollout. Gigaclear has also committed to delivering to [X] properties by [X], yet is unique in this commitment as Gigaclear will serve purely rural areas; the vast majority of which are only served by the BT Openreach network. This activity will then inject competition into areas that have never before been offered a competitive choice of wholesale network.

The scaling up of alternative network operators is then a welcome, recent phenomenon – which promises to inject competition into a fixed telecoms industry that has been dominated by a single national incumbent for a generation. However much of this is still just a promise; only recent improvements in delivery technology have made FTTP delivery viable in rural areas at scale.

Should BT then be successful in using targeted wholesale price reductions to increase take up on BT enabled retail services, it could effectively eat into the market segment that had been most likely to churn to the alternative network – result in descopeing and scaled back investment.

We then urge Ofcom to continue with its proposal of introducing ex-ante regulation through expanding the definition of ‘undue discrimination’ to prevent BT from introducing regionally targeted wholesale price reductions in order to undermine competitor networks.

Strategic Upgrading

Regarding the second bullet point, Ofcom discuss the threat of such activity within the consultation, but offer no means of addressing this threat. Rather, the consultation moves on to only propose a remedy to address the threat of regionally targeted wholesale price reductions.

This is concerning – as [X], the risk of strategic upgrading is greatest where network rollout is supported by state aid, which requires the designation of properties to be broadly determined prior to the selection of the successful network operator. In scenarios where BT bids for such schemes (such as through the BDUK programme) and is ultimately unsuccessful, BT is at that point well informed as to where the successful applicant intends to rollout to. The delivery process around such schemes can be cumbersome, often requiring two to three years before works are complete, depending upon the size of the intervention area. There is then a large window within which BT can act to undermine competition and choose to commercially fund upgrades to the relevant area.

As an FTTP network operator and the UK’s most successful BDUK applicant after BT itself, Gigaclear is then uniquely exposed to the risk of strategic upgrading.

To address this risk, we ask that Ofcom consider that where non-incumbent network operators are successful in securing state aid for network upgrades, BT Openreach is denied from upgrading its infrastructure within the relevant intervention area for the following three years.

Such an intervention places no undue burden upon BT Openreach, as to require state aid to roll out to a defined area indicates that commercial roll out alone would not be viable. Should BT Openreach then be unsuccessful in acquiring the BDUK contract, it should then

have no commercial basis for seeking to upgrade infrastructure in the area. The only purpose would then be to strategically undermine the business case of the alternative network looking to rollout their infrastructure in that area. This intervention then only targets activity that leverages incumbency to undermine effective competition.

We then ask that Ofcom consider this further protection when considering how to promote competition at a wholesale access network level.