



## Ofcom Call for Inputs - Openreach Proposed FTTP Offer starting 1 October 2021

### Non-Confidential Version

## 1. Introduction

- 1.1 KCOM Group Limited ('KCOM') welcomes the opportunity to provide comments on Openreach's proposed 'Equinox' FTTP offer.
- 1.2 On 1 July 2021, Openreach notified both Ofcom and its customer base of a proposed offer in relation to FTTP pricing ('the Equinox Offer').<sup>1</sup> Openreach is required to give 90 days' notice to Ofcom and its customers in relation to price changes, including offer pricing.
- 1.3 On 2 July 2021, Ofcom issued a Call for Inputs in relation the Equinox Offer asking Communication Providers ('CPs') to raise any initial concerns with Ofcom.<sup>2</sup>
- 1.4 KCOM has significant concerns in relation to the Equinox Offer. We consider it raises sufficient competition concerns to warrant further consideration by Ofcom with a view to determining whether to issue a direction to prevent the offer. Our response sets out our concerns.

## 2. Summary

- 2.1 In the Wholesale Fixed Telecoms Market Review 2021-2026 ('WFTMR') Ofcom has stated that it is looking to encourage investment in multiple FTTP networks. It considers that in doing so it is promoting the interests of citizens and consumers. It considers that infrastructure- based competition should bring benefits to consumers through innovation, choice, pricing, and higher quality of service.<sup>3</sup>

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<sup>1</sup> <https://www.openreach.co.uk/cpportal/updates/briefings/ultrafast/nga201721>

<sup>2</sup> [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0023/221378/call-for-inputs-openreach-proposed-ftp-offer.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0023/221378/call-for-inputs-openreach-proposed-ftp-offer.pdf)

<sup>3</sup> Ofcom, Promoting competition and investment in fibre networks: Wholesale Fixed Telecoms Market Review 2021-26 ('WFTMR Statement'), March 2021, Volume 1, paragraph 2.8-2.9 . Available at: <https://www.ofcom.org.uk/consultations-and-statements/category-1/2021-26-wholesale-fixed-telecoms-market-review>



- 2.2 Openreach's Equinox Offer strongly disincentivises CPs from using alternative FTTP networks. In turn, this reduces the incentive for alternative FTTP network operators to make additional investments in FTTP.
- 2.3 We consider that the Equinox Offer is detrimental to the investment incentives for alternative network operators and should therefore be rejected:
  - 2.3.1 The Equinox Offer disincentivises CPs from using alternative network operators;
  - 2.3.2 The Equinox Offer reduces the incentives for alternative network operators to expand their network;
  - 2.3.3 The Equinox Offer reduces the investment incentives for alternative FTTP network to invest in rural areas;
  - 2.3.4 The Equinox Offer is effectively a form of geographic pricing;
  - 2.3.5 The Equinox Offer disproportionately benefits BT retail as it is able to align its strategy to that of Openreach;
  - 2.3.6 The Equinox Offer has the impact of reducing competition in non-FTTP areas;
  - 2.3.7 The Equinox Offer could have long-term negative consequences on the development of infrastructure-based competition.
- 2.4 As such we consider that the Equinox Offer is likely to have a significant impact on alternative FTTP network operators. We are unable to comment as to whether the Equinox Offer brings 'significant benefits' as we do not have sight of BT's financial incentives.
- 2.5 We consider that on the basis of Ofcom's analytical framework that Ofcom should reject the Equinox Offer as it is likely to have a material impact on alternative FTTP network operators and act as a disincentive for them to make further investments in alternative FTTP networks.



### 3. KCOM response

#### Ofcom analytical framework

- 3.1 In the Wholesale Fixed Telecoms Market Review 2021-2026 ('WFTMR') Ofcom set out its analytical framework for assessing whether Openreach's commercial terms were likely to be approved or rejected by Ofcom.<sup>4</sup>
- 3.2 Ofcom states that where Openreach's commercial terms potentially create a barrier to using alternative networks then it will determine that these commercial terms would only be justified where:
- a) *the impact on nascent network competitors is unlikely to be material; and*
  - b) *the arrangements will generate clear and demonstrable benefits, such as:*
    - i) *the arrangements are essential to Openreach's business case for fibre roll-out; or*
    - ii) *the arrangements are necessary to offer more efficient prices that would deliver benefits for consumers.*<sup>5</sup>
- 3.3 We now set out below why we consider that Openreach's Equinox FTTP offer will have a material impact on alternative network investors, such as KCOM.

#### KCOM's response

- 3.4 Ofcom has previously stated that it wants to incentivise investment by alternative FTTP networks in order to drive infrastructure-based competition, because it considers that this is in the interest of citizens and consumers in the UK. The Equinox Offer has the exact opposite effect to incentivising infrastructure-based competition.
- 3.5 **The Equinox Offer disincentivises CPs from using alternative network operators:** The Equinox Offer encourages CPs to favour Openreach FTTP over Openreach's ADSL and FTTC networks. CPs must hit the 80% target to obtain lower FTTP rental prices.
- 3.6 The effect of this is that it also incentivises CPs to favour the Openreach FTTP network over alternative FTTP networks. For example, assume a CP has the ability to connect 100 end customers. If all end customers are on the Openreach network it must convert 80% of these. If 10 are on alternative networks, then in order to reach the 80% target (of 90 customers) it must convert 72. In total the CP must therefore convert 82 customers to

<sup>4</sup> WFTMR Statement, Volume 3, paragraph 7.154-7.172

<sup>5</sup> WFTMR Statement, Volume 3, paragraph 7.154



Openreach FTTP. Therefore at the margin, each customer converted to alternative FTTP networks makes it harder to achieve the Openreach target. This therefore disincentivises CPs from using alternative FTTP networks.

- 3.7 Ofcom itself says that exclusivity discounts (where discounts are conditional on a CP providing all or most of its requirements from Openreach) are *“likely to undermine alternative network expansion and undermine our goal of achieving network competition”*.<sup>6</sup>
- 3.8 The effect of the Equinox Offer is to incentivise CPs to maintain more connections on the Openreach FTTP network compared to alternative FTTP networks, as this makes it easier for CPs to meet the share requirements.
- 3.9 **The Equinox Offer reduces the incentives for alternative network operators to expand their network:** As stated above, the Equinox Offer encourages CPs to commit more of their volume to the Openreach FTTP network compared to alternative FTTP networks. All things being equal, alternative FTTP networks could expect to have lower volumes than would otherwise be the case. As a significant majority of the costs of an alternative FTTP network are fixed this acts as a strong disincentive to invest in FTTP.
- 3.10 Openreach’s overall strategy may also limit the ability of alternative FTTP network operators to compete effectively. Openreach has indicated that it plans to reach 25m premises passed by 2026. However, within those areas Openreach has made no firm commitment as to how it will roll out. In a specific geographic area, Openreach could cherry-pick the best locations covering 40-60% of homes making it very challenging for network operators to compete with the Openreach FTTP network.
- 3.11 **The Equinox Offer reduces the investment incentives for alternative FTTP network to invest in rural areas:** One model for investment is to invest in prosperous market towns and then ‘fill in’ network coverage in more rural areas. If the Equinox Offer has been in place in these more urban areas, it becomes far more challenging for alternative FTTP network operators to obtain the levels of subscribers necessary to make the investment case to provide coverage in adjoining rural areas and consequently will have negative consumer impacts.
- 3.12 **The Equinox Offer is effectively a form of geographic pricing:** In order to meet the share requirements of the Equinox Offer, a CP has to focus its effort in acquiring Openreach FTTP connections over Openreach ADSL/FTTC connections or connections on alternative FTTP networks. Given the current level of Openreach FTTP network, the only way of currently

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<sup>6</sup> WFTMR Statement, Volume 3, paragraph 7.166



achieving this is to focus all of activity on Openreach FTTP geographic areas and less on areas where there is no Openreach FTTP network.

- 3.13 CPs therefore have an incentive to focus on particular geographic areas where there is a high level of Openreach FTTP network. In effect this is therefore a form of geographic pricing and Ofcom has expressly prohibited geographic discounting.
- 3.14 The impact is compounded by the fact that alternative FTTP network operators typically have actual or planned network rollout in specific geographic areas. In certain geographic areas, Openreach's FTTP network is geographically close to that of other operators. Alternative network providers therefore face competition in limited geographic markets and the Equinox Offer makes it more likely that CPs will concentrate their marketing efforts in specific geographic areas and use the Openreach FTTP network rather than alternative FTTP networks.
- 3.15 **The Equinox Offer disproportionately benefits BT retail as it is able to align its strategy to that of Openreach:** Although Openreach is legally separated from BT retail, BT as a whole has an incentive to align the Openreach strategy with that of its retail arm. Given the current level of the coverage of Openreach's FTTP network, as a national operator BT retail is unlikely to initially meet the Equinox Offer requirements. However, as the Openreach coverage increases, BT retail will have a stronger incentive to meet the terms of the Equinox Offer, allowing it a greater ability to compete in the retail market. This has the effect that Openreach and BT retail become more strategically aligned when it is Ofcom's intention that the strategies of Openreach and BT retail should be more independent.
- 3.16 BT retail is discouraged from using alternative FTTP networks as it too is incentivised to ensure most of its FTTP growth remains on the Openreach FTTP network.<sup>7</sup>
- 3.17 Other large CPs could also align with the Openreach strategy and focus their efforts on converting customers to Openreach FTTP. However, if this does not align with their overall strategies, perhaps due to legacy investments, other large CPs will be placed at a disadvantage as their strategies will be aligned to Openreach / BT retail. Uniquely, BT group has the advantage of being vertically integrated, whereas other large CPs are not.
- 3.18 **The Equinox Offer has the impact of reducing competition in non-FTTP areas:** As discussed above, CPs will have an incentive to focus on FTTP areas. Given the disincentive to add customers to FTTC / ADSL networks, this may cause them to focus less on competing

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in non-FTTP areas. In extremis, firms could cease to compete for ADSL / FTTC customers at all.

- 3.19 The effect of this is to have competition focussed on Openreach FTTP areas, with less competition elsewhere. This may lead to a two-tier market structure where consumers without access to Openreach FTTP face the double negative of lacking access to FTTP as well as facing an overall lower level of competition.
- 3.20 **The Equinox Offer is likely to have long-term negative consequences:** As stated above, the effect of the Equinox Offer is to reduce the incentive for CPs to use alternative FTTP networks. This consequently leads to reduced incentives to invest. The overall effect is that there will be less infrastructure-based competition and lower overall levels of rollout. Alternative network operators could also withdraw from the market. The lower levels of network coverage goes against Ofcom's stated policy outcome, leading to worse outcomes for consumers in the long-run.
- 3.21 The consequence of this is that the government support required to build to the least profitable areas will be higher than it otherwise might have been. If this government support is not available, or is delayed, this will be detrimental to consumers, who might otherwise have obtained access to FTTP networks sooner.
- 3.22 Fundamentally the Equinox Offer reduces the incentive for alternative FTTP network operators to invest. Therefore, fewer consumers will be able to obtain access to alternative FTTP networks, leading to overall lower levels of coverage.

### Next Steps

- 3.23 In the WFTMR Ofcom sets out the process it will use to consider whether we should use its direction making powers in relation to commercial terms where the price or other contractual conditions are conditional on the volume and/or range of services purchased.<sup>8</sup>
- 3.24 We consider that the requirement to meet a particular share target incentivises firms to favour Openreach over other FTTP networks, thus reducing the ability of alternative operators to recover their cost.
- 3.25 We believe that Openreach's Equinox offer raises significant competition concerns and warrants further action by Ofcom. In particular:

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<sup>8</sup> WFTMR Statement, <https://www.ofcom.org.uk/consultations-and-statements/category-1/2021-26-wholesale-fixed-telecoms-market-review>, Annex 11



- (a) there is the potential for the offer to have a material impact on the rollout and competitiveness of alternative network infrastructure; and
- (b) it is not obvious that the arrangements will generate clear and demonstrable benefits.

3.26 We consider that Ofcom should not allow Openreach to go ahead with the Equinox Offer as it currently stands.

3.27 We urge Ofcom to act quickly to consider the potential implications and determine whether action in the form of a direction to prevent the offer is appropriate. While the threat of the offer remains, it is likely to have an adverse effect on alternative infrastructure providers, both in terms of their planned network deployment and their ability to compete with Openreach in already deployed areas.