



## BT's response to Ofcom's consultation document

*“Review of the wholesale broadband access markets 2006/07*

*Identification of relevant markets, assessment of market power and proposed remedies*

*Explanatory Statement and Notification”*

14 February 2008

BT welcomes comments on the content of this document, which is available electronically at <http://www.btplc.com/responses>

Comments should be addressed to:

Mike Fox, BT Group Regulatory Affairs, ppC8J BT Centre, London, EC1A 7AJ

e-mail [mike.p.fox@bt.com](mailto:mike.p.fox@bt.com)

## Executive summary

- BT strongly supports Ofcom's proposal to define separate geographic markets for wholesale broadband access in the UK. We agree that the scope of Market 3 should be extended: this is entirely justified by the dramatic changes even in the relatively short period since the last consultation, which has seen LLU take-up soar by 160% to almost 4 million unbundled lines at January 2008.
- We believe that in formulating its proposals on retail market definitions, Ofcom could have investigated more thoroughly the evidence for geographic markets at the retail level. In our view, the results of such work would reinforce the clear case for geographic markets at the wholesale level.
- Ofcom propose that no provider has SMP in Market 3. In our view, this conclusion is incontrovertible. We estimate that BT's share of this market may already be at or below the level at which single dominance concerns arise under competition law, and barriers to expansion are low, with all players able to benefit from economies of scale, scope and density.
- As explained in our response to the first consultation, we do not believe it would be legitimate for SMP remedies to be maintained in Market 3 for twelve months following the removal of SMP. If Ofcom proceeds with this proposal, any maintained obligations should apply only within strict limitations. BT would be willing to explore voluntary assurances to industry as a pragmatic, 'light touch' alternative to formal obligations.

## BT's responses to Ofcom's questions

Question 1: Do respondents have any comments, additional to those made in their responses to the November consultation, on Ofcom's approach and conclusions on market definition as set out in Section 3 of this document?

BT would like to make a number of comments on Ofcom's approach to market definition at both the retail and wholesale levels. The main thrust of our comments on retail market definition is that in our view, the approach in the consultation document underplays the significance of and evidence for geographic markets. We believe a thorough investigation into the evidence for geographic markets at the retail level would provide further support for Ofcom's conclusions on geographic markets at the wholesale level.

### *Retail market definition – bundling and geographic markets*

In our response to the first consultation in this market review, we suggested that the analysis in the consultation document gave insufficient recognition to the impact of bundling on the definition of the retail broadband product market. In its comments on retail bundling in the current consultation, Ofcom provides evidence that the availability of bundles to consumers varies by geography but concludes that:

*"...it is not clear at this time whether there are indeed separate retail geographic markets in the UK (excluding the Hull area) on a forward-looking basis as a sizable majority of retail broadband customers are provided service by ISPs that are currently maintaining a national pricing policy. In any case...for the purpose of this review it is not necessary for Ofcom to conclude on the precise scope of the retail geographic market."*

BT would caution against these conclusions for three reasons:

First, the fact that consumers can 'unpick' the BT offerings<sup>1</sup> does not in our view constitute sufficient grounds to conclude that such bundles do not form a product market. This is an important issue in the delineation of wholesale market boundaries given that this is informed by the market definition at the retail level.

Second, BT believes that there is strong *a priori* evidence to support separate geographic markets at the retail level, with the differentiating factor being the availability of different numbers and types of bundles to consumers. Even if all ISPs' headline prices for their stand-alone broadband services were national (which they are not), the differences in the geographic availability of bundles, with different implied 'embedded' prices for broadband would mean that broadband was effectively offered to consumers at different prices in

---

<sup>1</sup> Paragraph 3.105

different geographies. The fact that there are differences in many CPs' headline prices further reinforces this point. We believe these differences at the retail level support the case for separate geographic markets at the wholesale level.

The case for geographic retail markets is supported by evidence in Ofcom's most recent international comparison report entitled "The International Communications Market 2007" and published in December 2007. This document includes statements that, taken together, lead to the conclusion that geographic retail markets exist. Examples are given below:

- "...in Q1 2007...52% of people in the UK with broadband purchased it in conjunction with another communications service, thereby often receiving heavy discounts on the price of stand-alone broadband."<sup>2</sup>
- "...communications services ... are increasingly being delivered as multi-service propositions (examples in the UK include the 'free' broadband offer with TalkTalk's voice service, or Sky's See, Surf, Talk 'triple-play' offer which provides TV, voice and broadband, or Virgin's 'quad-play' offer which includes TV, voice, broadband and mobile.)"<sup>3</sup>
- "...'bundled' service offerings are typically not available to all consumers as they are generally geographically constrained to areas where premises are connected either to a cable network or to an unbundled telephone exchange."<sup>4</sup>

Third, whilst we agree it is not necessary for Ofcom to conclude on the *precise* scope of retail geographic markets for the purpose of this review, greater prominence should be attributed to this development since its dynamic has been pivotal in the development of geographic markets for wholesale broadband access.

#### *Retail market definition – additional comments*

We would also like to offer the following comments on retail market definitions.

BT would only agree partially with Ofcom's view that bundling of different services at the retail level would create complementarities rather than substitution at the wholesale level<sup>5</sup>. In fact, the extent of complementarity rather than substitution depends critically on the technical capability of the network; the cable network for example has long been capable of delivering multiple services. Further, the distinction between services across broadband networks and internet itself is increasingly blurred. In general, BT sees a growing level of direct substitution between networks including, for mass market consumers, substitution of voice away from fixed to mobile.

With regard to the methodological issue of the treatment of indirect constraints, BT would like to record its complete agreement with Ofcom's approach of including LLU operators and

---

<sup>2</sup> Section 4.1.8

<sup>3</sup> Section 1.4.1

<sup>4</sup> Section B.10

<sup>5</sup> Paragraph 3.193

cable at the retail stage for the reasons set out in paragraph 3.172. In passing, it should however be noted that the studies which Ofcom cites in paragraph 3.164 cast considerable doubt on the appropriateness of using a SSNIP test in a vertical chain of production of complementary activities.

#### *Wholesale markets*

We would also like to make two comments on geographic market definition at the wholesale level.

First, the document makes reference to the concept of uniform national prices as a determinant of a single national market. Ofcom do not pursue idea in the document, on the grounds that wholesale broadband access prices vary on a geographical basis. Nevertheless, we would like to place on record BT's view that where uniform national pricing has been mandated by a regulator, its existence should not then be used to deduce that a market is national.

Second, and most importantly, we would like to note BT's agreement with Ofcom's decision to expand the scope of the proposed Market 3 from 784 to 1070 exchange areas. This has the effect of expanding the coverage of Market 3 in terms of delivery points by just over ten percentage points, from 54.4% to 64.8% of UK homes and businesses. Given the dramatic 160% increase in LLU take up from 1.5 million lines at the end of January 2007 to 3.9 million lines at the end of January 2008, this is entirely justified.

Question 2: Do respondents have any comments, additional to those made in their responses to the November consultation, on Ofcom's proposed market power findings for the Hull area, Market 1 or Market 2?

BT has no further comments on these questions.

Question 3: Do respondents agree with the approach set out by Ofcom for its market power assessment in Market 3 and its conclusion that there is no SMP?

The statistics set out in paragraph 4.146 *et seq.* of the consultation document indicate that BT's market share in Market 3:

- fell below the threshold of 50% above which dominance may be presumed according to case law some time during late 2006 or early 2007;
- is on a downward trajectory, with significant declines in only the last two years; and
- looks set to dip below the 40% at which single dominance concerns usually arise by mid-2008, if indeed this level has not been reached already.

Ofcom also notes the significant factors indicating that sunk cost and economies of scale, scope and density are not barriers to entry and expansion in Market 3, notably the facts that:

- LLU operators do not have to incur the costs of provisioning an access network since they can purchase LLU inputs from BT;
- These inputs are covered not only by SMP remedies applying to BT in the upstream wholesale local access market which is upstream of the wholesale broadband access market, but also by enforceable commitments contained in BT's Undertakings to supply them on an Equivalence of Inputs basis;
- BT's economies of scope relating to access networks are also available to LLU operators, as these are reflected in BT's regulated LLU charges;
- LLU operators and Virgin Media can expand their services to new customers in areas where they are already present without incurring further significant sunk costs;
- LLU operators and Virgin Media can derive economies of scope in their abilities to offer bundled packages using already existing customer service and marketing functions;
- All 'Principal Operators' in Market 3 have similar access to capital markets such that no operator has an advantage in this respect over others<sup>6</sup>.

In light of these facts, we believe it is incontrovertible that BT does not have a "position of economic strength affording it to behave to an appreciable extent independently of competitors, customers and ultimately consumers<sup>7</sup>" in Market 3. We therefore agree with Ofcom's conclusion that BT does not have SMP in this market.

Question 4: Do respondents have any comments, additional to those made in their response to the November consultation, on Ofcom's proposed regulatory remedies for the Hull area, Market 1 or Market 2?

BT has no further comments on the proposed remedies in these markets.

Question 5: Do respondents agree with Ofcom's proposals in relation to providing affected parties with a period of notice prior to the removal of certain SMP services conditions in Market 3? In particular, do respondents agree with the proposed notice period and the proposed SMP service conditions to which the notice period applies?

In the first consultation, Ofcom stated that if it were to propose in the second consultation that BT did not have SMP in Market 3, it would need to consider whether existing regulation

---

<sup>6</sup> In support of this conclusion, we would note that two of the six Principal Operators other than BT belong to groups with market capitalisation over twice and three times respectively that of BT, and that one of these is part owned by the government of another EU member state.

<sup>7</sup> Framework Directive, Article 14(2)

should be maintained for a transitional period prior to formal revocation. The rationale for this would be to address the disruptive effects of a removal of regulation on BT's wholesale customers, in particular smaller ISPs.

In our response to the first consultation, we set out our view that there is no legal basis for the maintenance of SMP obligations following the removal of SMP, particularly in the light of:

- the requirement of Article 16(3) of the Framework Directive that National Regulatory Authorities withdraw SMP obligations where a market is found to be effectively competitive; and
- the requirement of Section 84(4) of the Communications Act that “where on, or in consequence of, a further analysis under this section, OFCOM determine that a person to whom any SMP conditions apply is no longer a person with significant market power in that market, they must revoke every SMP services condition applied to that person by reference to the market power determination made on the basis of the earlier analysis.”

We also gave our view that the final sentence of Article 16(3) of the Framework Directive, stating that “An appropriate period of notice shall be given to parties affected by such a withdrawal [of SMP obligations]” was intended to apply specifically where SMP was removed in the transition to the current regulatory framework and not where SMP is removed following subsequent Market Reviews.

BT therefore strongly maintains the view that there is no legal basis for the maintenance of SMP obligations following the removal of SMP. Even if the final sentence of Framework Directive Article 16(3) was intended to apply in these circumstances, we do not believe it could legitimately apply to a period as long as the year proposed by Ofcom.

If Ofcom nevertheless intends to proceed with the current proposal, we believe that any maintained obligations should apply only within the strict limitations described below.

*Restriction to DataStream only*

- If obligations are maintained, they should only apply to wholesale broadband access products covered by the SMP determination made at the conclusion of the previous Market Review.
- We believe the only such product is the existing DataStream product: paragraphs 1.21 to 1.23 of Ofcom's May 2004 Statement published at the end of the previous Wholesale Broadband Access Market Review clearly show that IPStream and BT Central were considered to be downstream of wholesale broadband access and therefore not in the market covered by the SMP designation and conditions.
- We would also stress that any maintained obligations should only apply to DataStream itself and not to any Next Generation Network successor product: since the intention would

be to safeguard those already using current products for a transitional period only, we do not believe there would be any case for extending them to products which have not yet been launched.

*Restriction to existing supply arrangements*

- As the purpose of any maintained obligations would be to safeguard existing customers in Market 3, such obligations should only cover DataStream supplied under contracts already in force when SMP is revoked.
- To provide reassurance to existing customers, BT would be willing to consider giving assurances on prices for DataStream supplied under such contracts during the transitional period.

*Obligations to be maintained*

- Under the current proposals, five of the seven existing wholesale broadband access SMP conditions would be maintained in force in Market 3 for one year following the removal of SMP. These are Conditions EA1 "Requirement to provide Network Access on reasonable request", EA2 "Requirement not to unduly discriminate", EA4 "Requirement to notify charges terms and conditions", EA5 "Transparency as to quality of service" and EA6 "Requirement to publish technical information".
- Only the two conditions relating to new supply, Conditions EA3 "Requirement to publish a reference offer" and EA7 "Requests for new Network Access" would be revoked immediately.
- We would suggest that any maintained obligations could be limited to EA1: we believe contractual obligations make Conditions EA4 and EA6 unnecessary, and that Condition EA2 would be unnecessary if the contractual obligations were combined with a price commitment from BT as suggested above. The obligations in Condition EA5 are only activated on direction by Ofcom, and no such direction has been made since the condition was first imposed in 2004. We therefore consider that perpetuation of the conditions other than EA1 would be disproportionate.

BT hopes that Ofcom will reconsider its proposals for the maintenance of SMP obligations in Markets 3, taking into account the comments and suggestions set out above. Removing, or at least limiting the number and scope of, these obligations would send a clear signal that Ofcom was committed to stripping away regulation no longer justified by competitive conditions in line with the principles of the regulatory framework.