5 June 2007

Amendment to charge control on Mobile Network Operators

T-Mobile's response

T-Mobile welcomes the opportunity to respond to Ofcom's unexpected consultation on the "Amendment to charge control on Mobile Networks Operators", dated 27 march 2007.

EXECUTIVE SUMMARY

1. T-Mobile has serious reservations about Ofcom's timing and the methodology of this consultation. Ofcom should have treated this issue within the 2-year-long Market Review Consultation process and not quite unexpectedly at the end of the review. Ofcom has conceded that the issue is not new. During the 2-year Market Review an amendment to the change controls was not proposed by any of the operators or discussed by Ofcom. We therefore regard Ofcom's approach as unreasonable: it undermines the market review process and reduces regulatory certainty.

2. T-Mobile believes that ultimately it is the Mobile Number Portability (MNP) Review that should deal with all issues related to Number Portability, including that of the termination rates attached to ported numbers. In addition, Ofcom should give priority to solving the disputes which have arisen in the context of that framework rather adding distortions to a different piece of regulation.

3. T-Mobile remains of the view that it is Ofcom's discriminatory regulation that allows H3G to charge significantly higher termination rates than the other operators that is causing distortions in the market and with respect to ported numbers. Ofcom's proposals risk adding an additional distortion in the market to the sole advantage of one operator. T-Mobile regards this approach as discriminatory.

4. Ofcom's proposal to intervene and implement Option 4 is detrimental to consumers, implies extra costs for the industry and for consumers while providing no benefits. Ofcom has not attempted to assess the impact of its proposals, which it is required to do by the Communication Act.

5. Since H3G has distorted the market for years by setting very high termination rates, and will continue to do so even in light of the newly-determined regulated rates, Ofcom should not proceed with its proposal to implement Option 4, which risks distorting the market even more.

6. T-Mobile therefore supports Ofcom's Option 1, i.e. 'Do Nothing'.

GENERAL COMMENTS

1. Ofcom's Market Review process

Ofcom has just completed a 2-year market review of call termination charges. Ofcom and the five operators affected have worked closely and at least two market review consultations were published by Ofcom. The issue of amending the price control to deal with MNP was not mentioned in the course of the 2-year review, not by Ofcom nor by any of the other operators in their public responses[1].

Operators have a legitimate expectation that the review would provide stability in the call termination market for four years. Ofcom has instead worked for two years without mentioning this issue, and has then decided to publish this consultation without informing operators about its intention to do so prior to its publication. At a minimum, Ofcom had been aware of its willingness to intervene in this matter since November 2006, when Ofcom received the operators' final responses to the Market Review consultation, but it did not communicate its intention to consult on such a major change in regulation in the subsequent meetings held with operators.

Given that under-recovery is not a new issue and no significant changes have occurred in the market, it seems extremely inappropriate to immediately consult on changing the outcome of a 2- year market review, which was intended to create stability for 4 years.

Ofcom claims H3G has raised the issue of amending the charge controls to account for ported numbers in their responses to Ofcom market review consultations.

T-Mobile has found no evidence of this. Rather, from H3G's responses to Ofcom it clearly emerges that, like T-Mobile, H3G believes the most appropriate way to look at MNP issues is through the MNP consultation process. H3G state:

> *"This is a matter around the appropriateness of the existing MNP arrangements and cannot be used as a justification to reach inappropriate conclusion on call termination charge controls.*
>
> *Ofcom should be addressing the root cause of the problem, not introducing further work around solutions, which will become increasingly unsustainable and inefficient.[2]"*

Ofcom is in fact doing the opposite. By suggesting a manipulation of the rates, Ofcom is adding another distortion in call termination regulation, and one that will bring clear advantage to one operator only, while damaging consumers overall.

T-Mobile therefore regards Ofcom's timing and proposed actions as inappropriate, not least because Ofcom is sending a clear signal that they believe they have the right to intervene and change a major piece of regulation without appropriate notice. This is extremely risky for investment decisions, in particular since Ofcom's proposal comes at the very beginning of the new regulatory period, when operators are trying to

[1] As we explain below, not even H3G in its responses proposed to amend the charge controls structure to include ported numbers.
[2] H3G's response to the March 06 Call Termination Review, page 4

incorporate information on the incentives provided by the newly created regulation on their internal performance. This process risks sending perverse signals about Ofcom's intention to intervene in a supposedly stable environment.

In summary, we regard Ofcom's approach as unreasonable: it undermines the market review process and reduces regulatory certainty. Ofcom should therefore not intervene at this time.

2. The Mobile Number Portability Review

T-Mobile believes the Mobile Number Portability (MNP) Review should deal with all issues related to Number Portability.

The current MNP arrangements have existed in the UK for almost 10 years. All operators have had to deal with MNP on the existing basis and have found the most efficient solution. These technical arrangements were well known to H3G before their entry in the market. It was also well known that the current arrangements have an impact on wholesale call termination revenues.

Ofcom should not just change part of the arrangements without analysing the impact of this change on the overall MNP framework. Operators have put significant effort into working with Ofcom and amongst themselves to analyse the current framework. Operators have not as yet been made aware of Ofcom's conclusions.

In addition, a number of disputes relating to Number Portability have recently been raised against mobile operators, including one by H3G[3]. We strongly urge Ofcom to give priority to solving these disputes in a consistent manner rather than wasting resources in complicating an already existing and complex piece of regulation.

3. Ofcom's Call Termination Regulation remains discriminatory

T-Mobile remains of the view that the newly determined termination rates discriminate in favour of H3G, which was allowed a higher margin on its incurred costs. H3G's rates will therefore continue to distort the mobile market.

H3G has been over-recovering on termination rates for years: this is clearly illustrated by H3G's "WePay" tariff, under which customers, in addition to standard subsidies in place in the market, have been given 5ppm of credit for every call they receive. This was roughly the difference between the regulated termination rates of the other operators and H3G's previously unregulated rate. This created massive distortions in the mobile market.

[3] H3G has also threatened another dispute which would make Ofcom's proposed changes otiose.

Even under the new regulation in force since April 2007, H3G's regulated rates are well above the market call termination rates. Ofcom has decided to allow a glide path whereby the margin between H3G's LRIC and the incurred costs is higher than the margin allowed to other MNOs on their LRIC costs. This means H3G's regulated rates will continue to distort the market.

Ofcom states that across the market the percentage of ported-in minutes does not differ significantly among operators. This means it is therefore only the level of the termination rates and not the relative magnitude of ported in volumes that matters for this determination. If H3G's rates were in line with the market rates the problem would affect all operators roughly in the same manner. Rather, Ofcom has decided to continue to discriminate in favour of H3G by allowing them much higher rates. If Ofcom had brought H3G's rates in line with the market average then this issue would have much more limited proportions. It is inappropriate for Ofcom to intervene now to put an end to a purported distortion that Ofcom itself created by setting H3G's rates out of line with the market average.

In conclusion, seeing as H3G has already distorted the market for years by setting very high termination rates, and will continue to do so in the future even with the newly determined regulation, Ofcom should not proceed with the current proposal which risks distorting the market even more.

4. Consumers would be worse off if Ofcom's Option 4 were implemented

Ofcom's proposal to intervene and implement Option 4 is detrimental to consumers.

Options 2, 3 and 4 all imply not only a transfer of resources from some operators to others but also a pure loss for some operators, in particular fixed operators. Option 2 in particular highlights that current MCT revenues are insufficient to cover the impact of these proposals, and therefore any new arrangements would have to rely on additional resources taken away from consumers.

The extra costs of allowing some operators to increase their actual termination rates would be borne entirely by consumers with no benefits. Ofcom is wrong in assuming that these proposals will have beneficial effects on the operators' incentive to attract customers. The mobile market is a mature market and operators are targeting other operators' customers. The current MNP system has been extremely successful: consumer satisfaction is well illustrated by the high level of porting among churned customers. The wholesale pricing of ported calls is irrelevant in the customer's eyes and should be left to industry. Unless there are complaints from customers or evidence of consumer harm, there is no call for regulatory intervention. Also it is highly unlikely that both a new routing solution for ported numbers and an amendment to existing call termination rate structure would directly increase the number of people porting their number: from the consumers' perspective the porting process would not change. If consumers wish to port then they will do so regardless of the method and this behaviour would not change just because Ofcom has changed the structure of the wholesale rates.

In addition, Section 7 of the Communications Act requires Ofcom to carry out Impact Assessments in relation to proposals which are "important". The Act says a proposal is "important" if it would be likely to have a significant impact on persons carrying on businesses operating in markets Ofcom regulates or have a significant impact on the general public in the UK or a part of the UK. Ofcom "regards this as a minimum requirement and believes Impact Assessments form a key part of best practice policy-making"[4].

The proposals discussed in the consultation have a significant impact on both mobile and fixed operators and on the UK consumers. Yet Ofcom has not carried out a proper impact assessment of the proposals adopted. We regard this approach as unacceptable.

If Ofcom decides to depart from our suggested option, i.e. Option 1, T-Mobile urges Ofcom to publish a second consultation. This would need to include a detailed analysis of the extra costs imposed on operators and consumers. Ofcom should quantify the benefits that they believe consumers would get from these proposals. We submit that these benefits should be considered null, since as explained above customers would obtain no extra benefits were option 4 implemented, while they would entirely bear the extra costs of this proposal.

T-Mobile has already raised serious concerns about Ofcom's welfare analysis in the MCT Review[5]. We do not believe those concerned have been addressed properly by Ofcom in its statement. Yet we believe Ofcom risks reducing overall welfare if its proposal is implemented without even trying to measure its implications.

In conclusion, the proposals put forward by Ofcom imply extra costs for the industry and for consumers while providing no benefits. Ofcom has not attempted to assess the impact of its proposals, which is required to do by the Communications Act.

T-Mobile therefore asks Ofcom to reconsider its position on these proposals and, at a minimum, to carry out a detailed cost-benefit analysis of the four options proposed.

5. Ofcom's proposed options

In this consultation Ofcom provides four options as a solution to the differential termination rates attached to ported-in numbers.

T-Mobile supports Option 1, i.e. 'Do Nothing', for the following reasons:

- This issue was not raised during the 2-year Market Review nor was an amendment to the change controls proposed by any of the operators or by Ofcom. By raising this issue at the beginning of the new regulatory period Ofcom has undermined the validity of the Market Review consultation process and has sent a clear signal that operators should not expect regulatory stability for the new regulatory period.

- The issue of the termination rates attached to ported numbers must be solved within the MNP Framework, not in other consultations. By doing so Ofcom risks undermining also the validity of the MNP Framework consultation process.

[4] Better Policy Making Ofcom's approach to Impact Assessment, 21 July 2005
[5] See T-Mobile's response to Ofcom's Welfare Analysis Model, January 2007

- Ofcom's proposal would induce further distortions in the market and would increase Ofcom's discriminatory attitude toward H3G.

- It is H3G's termination rates that keep distorting the market, not the MNP arrangements. Ofcom's proposal risks adding an additional distortion in the market to the sole advantage of one operator. T-Mobile regards this approach as discriminatory.

- Ofcom's proposal is detrimental for consumers and does not provide additional benefits.

Therefore T-Mobile does not support Options 2, 3 and 4.

T-Mobile regards Option 2 as unreasonable. An inter-operator financial settlement system implies that operators would risk incurring a pure loss in order to compensate other operators who are allowed higher termination rates. As Ofcom correctly identifies, MCT revenues are insufficient to cover the transfers between operators. This highlights the fact that, given the structure of the MNP arrangements, any solution which departed from the existing situation would cause additional costs to the industry. In addition, an inter-operator financial settlement would prove extremely difficult to operate, and would cause additional regulatory costs.

T-Mobile also opposes Option 3. Ofcom does not provide a clear explanation of how the suggested complicated system would be implemented. Ofcom refers to a generic forecast level of ported-in minutes between each operator in each of the charge control years without detailing how Ofcom intends to obtain this information and agree it with the operators, and it does not clarify whether the growth rates of ported-in minutes will apply to the industry or will be operator-specific. In addition, if significant changes occur in the market these would not be accounted for in the forecasts. Ofcom is well aware of the problems it encountered in producing reliable forecasts during the last MCT Market Review. We would strongly recommend Ofcom should not go down the route of uncertain, debatable and unavailable forecasts again. In conclusion, Ofcom should stay away from such intrusive form of regulation, which, besides being based on uncertain data, provides no flexibility to the operators.

T-Mobile opposes Option 4. Option 4 would induce further distortions in the market and would increase the regulatory burden for operators.

Ofcom should always seek to intervene in the market with the least intrusive regulatory methods. The current termination charges represent a very intrusive regulatory method and we urge Ofcom not to make them even more intrusive by adding further distortions to the Target Average Charge formula.

Response to Ofcom's questions

Question 1: What are respondent's views on the appropriateness of Option 1 as a solution to the distortions created by the existing MNP mechanism on MCT?

T-Mobile supports Option 1, i.e. 'Do Nothing', for the following reasons:

- The issue of termination rates attached to ported numbers was not raised during the 2-year Market Review nor was an amendment to the change controls ever proposed by any of the operators or by Ofcom. By raising this issue at the beginning of the new regulatory period Ofcom has undermined the validity of the Market Review consultation process and has sent a clear signal that operators should not expect regulatory stability for the new regulatory period.
- The issue of the termination rates attached to ported numbers must be solved within the MNP Framework, not in other consultations. By doing so Ofcom risks undermining also the validity of the MNP Framework consultation process.
- Ofcom's proposal to implement Option 4 would introduce further distortions in the market and would increase Ofcom's discriminatory attitude toward H3G.
- It is H3G's termination rates that keep distorting the market, not the MNP arrangements. Ofcom's proposal risks adding an additional distortion in the market at the sole advantage of one operator. T-Mobile regards this approach as discriminatory.
- Ofcom's proposal to implement Option 4 is detrimental for consumers and does not provide additional benefits.

Question 2: What are respondent's views on the appropriateness of Option 2 as a solution to the distortions created by the existing MNP mechanism on MCT?

T-Mobile regards option 2 as unreasonable.

An inter-operator financial settlement system implies that operators would risk incurring a pure loss in order to compensate other operators who are allowed higher termination rates. As Ofcom correctly identifies, MCT revenues are insufficient to cover the transfers between operators. This highlights the fact that, given the structure of the MNP arrangements, any solution which departed from the existing situation would cause additional costs to the industry.

In addition, an inter-operator financial settlement would prove extremely difficult to operate, and would cause additional regulatory costs.

Question 3: What are respondent's views on the appropriateness of Option 3 as a solution to the distortions created by the existing MNP mechanism on MCT?

T-Mobile does not support Option 3.

Ofcom does not provide a clear explanation of how this complicated system would be implemented. Ofcom refers to a generic forecast level of ported-in minutes between each operator in each of the charge control years without detailing how Ofcom intends to obtain this information and agree it with the operators, and it does not clarify whether the growth rates of ported-in minutes will apply to the industry or will be operator-specific.

In addition, if significant changes occur in the market these would not be accounted for in the forecasts.

Ofcom is well aware of the problems it encountered in producing reliable forecasts during the last MCT Market Review. We would strongly urge Ofcom not to go down the route of uncertain, debatable and unavailable forecasts again.

In conclusion, Ofcom should stay away from such intrusive form of regulation, which, besides being based on uncertain data, provides no flexibility to the operators.

Question 4: What are respondent's views on the appropriateness of Option 4 as a solution to the distortions created by the existing MNP mechanism on MCT? Question 6: What do respondents think about Ofcom's proposed amendment to the compliance formula?

For the reasons explained above T-Mobile does not support Option 4.

We regard the formula suggested by Ofcom as an additional complication to an already complicated and intrusive regulatory methodology. It is therefore entirely unnecessary.

Question 5: Do respondents agree with Ofcom’s conclusion?

As explained above, T-Mobile strongly disagrees with Ofcom’s conclusions.

In addition, before reaching its conclusion Ofcom should present a clear Impact Assessment to analyse the increased costs that the industry and consumers would bear. This analysis becomes even more compelling considering we do not foresee any advantages for consumers from Ofcom’s proposals.

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