Representing the Communication Services Industry

Charge control review for LLU and WLR services
Issued 31 March 2011

FCS response - 8 July 2011

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Introduction

The Federation of Communication Services represents over 300 businesses delivering products and services via wireless, copper and fibre technology. This response has been prepared on behalf of the Fixed Service Providers Group within the Federation. More than 150 FCS members consume WLR and related wholesale products to deliver services to end user customers. A list of FCS members can be found on the FCS website.

Overview

We welcome the opportunity of responding to this consultation on Ofcom's review of charge controls for LLU and WLR services. We agree with Ofcom's finding in its most recent reviews of the Wholesale Local Access and Wholesale Analogue Exchange Line markets that BT group continues to have SMP in both of these markets and with Ofcom's conclusion that BT should be required to continue to provide both WLR and LLU.

WLR is a key enabler for competition allowing a range of innovative products and service propositions to be developed by service providers and resellers who operate on both a volume and niche basis. The fact that WLR volumes lines currently stand at 6.2 million (in defiance of ongoing predictions of its decline) is an indicator of its ongoing value in the market.

This is particularly true for the SME customer, who needs flexibility and responsiveness to changing requirements, and this view is supported by the findings of research carried out by YouGov on behalf of FCS in the latter part of 2010 which demonstrates clearly that SME customers prefer to deal with independent and local resellers who can meet their needs better. It is essential therefore that WLR remains competitive with other wholesale products.

We would like to highlight 3 key issues arising from the review which are of potential concern to our fixed service provider members:

1. We have major concerns about the impact of the option identified by Ofcom in section 5.25, which proposes to allow the WLR transfer charge to rise over the life of the control to align with costs on either a CCA FAC or LRIC basis. This would see WLR transfer fee rise from the current level of £3.02 to either £16.00 or £11.00 depending on which cost base is used.

   Ofcom has correctly identified that such a quantum move in pricing, involving successive major year on year increases is likely to cause considerable disruption in the market. CP margins on rental are slim and in order to recover the increased cost of acquisition arising from such an increase CPs would be compelled to increase their charges to end user customers, to increase contract lengths (with associated early termination charges), or both.

   FCS members currently consuming WLR believe that such an increase would be a very significant barrier to switching and therefore damaging to competition and consumer choice. Ofcom should not pursue this approach.

2. We would like to challenge Ofcom's view, set out in sections 5.32 to 5.37 that the charge for MPF to WLR transfers at its current level of £34.86 does not cause distortion in the market. In fact, we believe that the low volumes of this type of transfer are a direct result of its cost. In our experience, neither the customer or the CP is willing to absorb this level of charge. In

the case of the CP this is because of a high level of risk that this cost may not be recovered during the life of the contract.

This is an issue which does not affect only residential consumers. We are aware of examples where business customers have been effectively prevented from moving to a new provider due to this. In an example cited by one FCS member the customer had 2,000 lines which had been moved to MPF. The customer wished to move back to a WLR provider but the aggregated cost of doing so (at almost £70,000) was prohibitive for both the customer and for a number of potential gaining providers who the customer had approached.

While we appreciate that the cost of both WLR to MPF and MPF to WLR transfers have been set on the basis of actual costs incurred by Openreach, it can be seen how such high charges can distort the market.

It would be a better approach to operate on the basis of a nominal or zero transfer charge for all CP to CP switches, regardless of the products and technologies involved, and to recover the costs of transfer via the monthly rental. In our view this is likely to lead to a more vibrant market.

3. We also note that Ofcom is not proposing to set a charge control for the WLR Premium rental charge. Although there has been some migration away from Premium lines since introduction of the option for a business directory listing as an option within the Core WLR product, numbers of Premium lines remain high and are a prerequisite for consumption of some line features, for example. number presentation.

   While there has been no increase by Openreach in the rental during the 18 months since the voluntary undertaking expired, we believe that Ofcom must continue to monitor the situation and be ready to intervene if there is any move to increase charges in this area.

As a final comment, we would like to note that the volume forecasts in Annex 6 predict a significant fall in the number of WLR lines by 2014. In our response to the previous review we indicated that we felt that these forecasts were over pessimistic, which in fact proved to be the case. We continue to believe that Ofcom is underestimating the ongoing demand for services based on WLR.

We have restricted our responses to the specific consultation questions to those issues affecting competition and WLR. For this reason, we have not provided answers to questions 3.5-3.11, and have omitted all questions in sections 4 and 7 as these relate either to the detail of LLU pricing or technical cost modelling issues.

Ofcom consultation questions

Question 3.1: Do you agree with Ofcom's proposal to set synchronised charge controls for LLU and WLR?

We agree. Although WLR and LLU are in separate markets in the regulatory sense, they are complementary wholesale inputs used by CPs with different business models to compete to provide services to end-users in the same target markets. For this reason it makes sense for the reviews to be conducted in parallel.

Question 3.2: Do you agree with Ofcom's proposal to set charge controls for LLU and WLR to expire on 31 March 2014?

We agree. In view of the rapid technology change which is taking place with the roll out of fibre, a three year period from the ending of the recently expired controls is the maximum for which the new charge controls should be set.

However, we suggest that Ofcom should be ready to intervene earlier to preserve a level competitive playing field if the pricing of new fibre based has a distorting impact on the market within the life of the new controls.

Question 3.3: Do you agree with Ofcom's proposal to use a CCA FAC methodology to establish the cost base for the next LLU and WLR charge controls? Please give reasons for your answer. (Note that respondents are also invited to comment on continuation of the RAV approach in Question 3.5 below.)

We agree that it make sense to continue to use the established methodology.

Question 3.4: Do respondents agree with our proposal to apply anchor product pricing as a guiding principle in setting the charge controls, whilst including economies of scope which result from the allocation of costs in our financial modelling? Please give reasons for your answer.

We agree with the proposed use of anchor product pricing and with Ofcom's analysis of the incentives this provides to ensure that the price of consuming products based on existing technology does not rise. We agree that this is especially relevant in light of the current investment in Openreach's new fibre network.

Question 3.5: Do you agree with our assessment that the decision on the treatment of pre-1997 duct assets set out in the 2005 Valuing BT's Copper Network remains appropriate for this set of charge controls? If not, why do you consider that the basis of valuing pre-1997 assets should change and what valuation basis should be used?

No comment.

Question 3.6: We note that we would expect that the difference between the charges for MPF and PIA should be at least as great as the difference in their respective incremental costs. Thus, if we maintain the RAV adjustment in copper based access services, we would expect that any assessment that we make of duct access charges would reflect a consistent approach to asset valuation, recognising the RAV adjustment. We consider this to be consistent with economic considerations and the European Commission's NGA recommendation. Do you agree with this assessment? of the need to recognise the RAV adjustment in the setting of duct access charges? If not, please give your reasoning.

No comment.

Question 3.7: Do you agree that it remains appropriate to value post-1997 assets on a replacement/CCA basis? If not, please give your reasoning.

No comment.

Question 3.8: Do you agree with our assessment that as BT's recent valuation of post-1997 assets is not consistent with alternative estimates of replacement values it does not form a appropriate basis for setting charges? If not, please give your reasoning.

No comment.

Question 3.9: Do you agree with our proposal to include a valuation of duct in the charge controls based on indexation of post 1997 expenditure? If so, should this indexation be based on RPI; GCSI or GCSI adjusted for either productivity, scale economies or both (the detailed examination of these indices is set out in Annex 4? Please give reasons for your answer.

No comment.

Question 3.10: Do you agree with our proposal to discount the indexed valued by an estimate of a national roll out of duct? If so, do you consider BT's estimate of 14.5% to be appropriate? If you disagree with our approach please give your reasons.

No comment.

Question 3.11: Our range for the duct value is defined by the degree to which BT is able to establish contracts with cost below the national average? Do you consider that it is reasonable to expect BT to achieve below national costs on average?

No comment.

Question 3.12: Do respondents agree with our preferred approach to use glide paths to align charges with costs except in the circumstances discussed above where oneoff adjustments may be preferable? Please give reasons for your response.

Yes. Glide paths avoid unnecessary disruption in the market.

Question 3.13: Do you agree with Ofcom's proposal to impose the arrangements for charge control compliance and requirements for provision of data set out in Annex 12? Please give reasons for your answer.

No comment.

Question 3.14: Do you agree with Ofcom's proposal to use the RPI as the appropriate measure of inflation for indexation? Do you agree that change in RPI for the year to 31 October preceding the start of each Relevant Year should be used? Please give reasons for your answers.

We agree.

Question 3.15: Do you agree with Ofcom's proposal to retain provisions for "Carry Over" in the new controls? Please give reasons for your answer.

No comment

Question 3.16: Do you agree with Ofcom's proposal that charge changes made under the new controls prior to April 2012 should be made with a minimum 28 days notice? Please give reasons for your answer.

We agree.

Question 3.17: Do you agree with Ofcoms proposal that charge ceilings for key services should be set for the 1st period of the new controls – i.e. the period between the first day of the new controls and 31 March 2012? Please give reasons for your answer.

We agree.

Question 5.1: Do you agree that the core rental should be subject to a charge control which sets the price of the WLR core rental on a glide path to ensure it recovers CCA FAC costs by the end of the charge control period?

We agree.

Question 5.2: Do you agree that WLR transfer should be subject to a separate charge control? Please give reasons for your answers.

We agree. As stated in the overview section, high levels of transfer charge can distort the market and Ofcom needs to retain the flexibility to manage the controls on transfer charges separately.

Question 5.3: Do you think that Ofcom should adopt Option 1 or 2 above as its approach to the pricing of WLR transfer during the next charge control? Please give reasons for your answer.

Option1. As note in our overview, FCS members currently consuming WLR believe strongly that a move to the level of transfer charge envisaged in Option 2 would create a very significant barrier to switching, damaging competition and consumer choice.

Question 5.4: Do you think that the cost orientation obligation should be removed from WLR transfer services? Please give reasons for your answers.

Yes.

Question 5.5: Do you agree that the price for WLR new provide should be subject to a separate control which ensures that the price is aligned with FAC by the end of the charge control period?

We agree.

Question 5.6: Do you agree that a charge control would not be practical for MPF to WLR conversion given the low volume of services.

We believe that the low volume of transfers is due to the current level of the charge. We believe that Ofcom should impose a separate charge control to reduce the MPF to WLR charge to a level closer to the WLR to WLR charge.

Question 5.7: Do you agree that charges for MPF to WLR conversion should not be aligned precisely to the charge for WLR to MPF?

As a matter of principle, we believe that transfer charges should be kept at a low level and Openreach costs from activity associated with the transfer should be recovered via the monthly rental.

Question 5.8: Do you agree that charges for calling and network features should not be charge controlled? Please give reasons for your answers.

We agree that the recent behavior of Openreach in this area has resulted in a number of special offers and price reductions, that a price control is not necessary and could even be counterproductive by constraining Openreach's flexibility in price setting in this area. Nonetheless, it may be prudent to apply some form of "safeguard cap" to prevent any unreasonable increases beyond current levels.

Question 5.9: Do you agree with that pre-validation charges should not be charge controlled? Please give reasons for your answers.

We believe that charges should not apply for this type of service. Costs should be recovered from the rental charge.

Question 5.10: Do you agree with that ISDN to WLR conversion charge should be subject to cost orientation obligation but should not be charge controlled? Please give reasons for your answers.

No comment.

Question 5.11: Do you agree with that cancellation charges should not be charge controlled? Please give reasons for your answers.

We agree that specific charge controls may not be appropriate but some form of safeguard cap and/or monitoring by Ofcom to prevent unreasonable increases would be welcome.

Question 5.12: Do you agree that time related charges should remain out of the scope of the charge control and subject to general remedies applied in the WAEL market review?

We agree that a cost orientation requirement is appropriate but some monitoring and guidance from Ofcom to avoid unreasonable increases would be welcome.